

NON-TRADITIONAL SOURCES OF FINANCING FOR SMALL AND MEDIUM BUSINESS ENTERPRISES IN A DEVELOPING ECONOMY CONTEXT

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Abstract

This study examines the role of Non-Bank Financial Services for Small and Medium-Sized Enterprises finance including venture capital, financial leasing, factoring and capital market. It explains the influence of policies, regulatory frameworks and institutional setups along with Egyptian Government's efforts in order to improve SMEs' access to finance as SMEs account for over 90 percent of active enterprises in Egypt and contribute to over 80 percent of GDP and 75 percent of total employment. Yet, they remain at a clear disadvantage vis-à-vis larger businesses.

Assessment of Egyptian NBFS using regulatory framework and standards for companies establishment and their activities founded that financial leasing, factoring and venture capital still have unremarkable role in Egyptian SMEs financing because of the lack of well-functioning and efficient means of registering and enforcing property rights, and limited and poorly available information on potential clients and borrowers.

Through evaluating the performance of listed companies on Nile Stock Exchange using financial ratios, the study suggests a positive relation between their risk ratios and profit ratios. Increase in companies' profit is considered a result of increase in risk, but many SMEs are still worried about the high risk of being listed on Nile Stock Exchange. The study reveals that there are three main pillars which are responsible for enhancing the environment surrounding NBFS. The first pillar is the increasing awareness about non-bank financial companies in Egypt. The second pillar is designing incentives for those companies and the third pillar is the need for capable, skilled and qualified fund management to secure the implementation of successful investment plans.

1. INTRODUCTION

SMEs are a dynamic force for sustained economic growth and job creation. They are a valid, crucial component of a vibrant industrial society. SMEs stimulate private ownership and entrepreneurial skills; they are flexible and can adapt quickly to changing market demand and supply conditions; they generate employment, help diversify economic activities and make significant contribution to export and trade. Egyptian SMEs face many challenges as they aspire to grow. One of the key challenges is access to finance with reasonable cost and requirements. In particular, many SMEs find it difficult to finance their production cycle. While banks already possess the resources to finance SMEs, they have to follow certain procedures and conditions, which should be implemented by SMEs if they want access to banks' finance (Elasrag (2013)).

Moreover, although Egyptian SMEs accounts for about 75% of employment, 80% of GDP and 99% of non-agricultural

private sector, about 75% of SMEs' applications and 92% of small firms' applications for banks' loans are rejected and only 6% of bank loans are granted to SMEs (Omran (2007)). Most enterprises are undercapitalized with a significant current account from associates in order to retain flexibility and family control. This prevents banks from lending unless they can obtain significant guarantees.

The issue of SMEs development ranks high among the government's priorities of socio-economic development. There have been more than 150 entities that provide technical and financial assistance as well as service delivery to this sector. However, these efforts have been scattered and largely uncoordinated, which has curtailed the sector's growth potential (EL-Hawary (2007)). Hence, the Government of Egypt (GOE) has embarked on significant regulatory and other reforms to open up global markets and improve the domestic investment environment for SME development. Increasingly, there are efforts to understand more about the barriers and constraints to SME in order to encourage and stimulate more growth-oriented entrepreneurial activity. This will require improved access to financing, information, business support services and technology, entrepreneurship education and SME training, reducing regulatory time and costs associated with starting up and operating SMEs, strengthening linkages between small and large firms and promoting a culture of entrepreneurship.

In Egypt, limited access to finance is considered a key constraint to the private sector growth. This is especially true for smaller firms that have minimal influence on policy reform. Besides, most people in the developing countries do not have access to financial services. Only very few benefit from saving accounts, loans or a convenient way to transfer money. NBFS have become a big issue in the world to solve the lack of access to financial services SMEs.

This paper examines the importance of NBFS as a source of SMEs' finance because non-bank finance like capital markets,

insurance, mortgage finance, financial leasing and factoring can serve as an important source of finance for SMEs. It also tries to keep record of all NBFS that can provide direct external finance for SMEs to assess the Egyptian experience by Regulatory framework and Standards of Establishing Companies and their activities. It discusses the Egyptian case study of the Nile Stock Exchange (NILIX) by explaining its role in improving the SMEs' access to finance, along with its new listing rules and regulations that focus on a cost-effective regulatory regime adapted to the needs and characteristics of SMEs.

The core of the research is built upon the objective that SMEs access to Finance could be enhanced if suitable NBFS are developed. For this, we aim to:

- Examine the role of NBFS in financing SMEs lifecycle
- Determine the organizational framework of NBFS in Egypt
- Build a matrix to clarify the Egyptian NBFS and actions taken by GOE to develop them
- Examine the role of Nilex by evaluating the performance of listed companies using financial ratios calculated from their financial statements

2. LITERATURE REVIEW

SMEs are the driving engine behind economic growth in Developing and Free-Market Economies. There is growing global appreciation in Egypt that SMEs play a critical role in the development, generating employment and supporting trade (Costin (2015)). The SMEs strategy is consistent and reflects the government's key objectives for development of the SME sector, specifically, the GOE's Long-Term Development Vision 2022, the Five-Year Plan for Socio-Economic Development 2002-2007, and the Government's Ten-point Action Plan (OECD (2010)).

In Egypt, NBFS such as financial leasing, factoring, venture capital and Nile stock exchange are regulated by specific rules such as 1995 Law No. 95 which regulate financial leasing and

minimum capital requirements for leasing companies, by 1997 Law No. 8 on Investment Guarantees and Incentives to identify services such as factoring, venture capital and stipulate the related rules, by 2009 Law No. 10 to regulate non-banking financial markets and instruments and create a single regulatory body called the Egyptian Financial Supervisory Authority (EFSA).

2.1 The Conceptual Framework of Research

Egyptian Definition of SMEs: Opinions vary among countries and within the same country on the definition of SMEs due to different definition metrics such as Work-Force Size, Capital, Annual Sales and Technical Expertise. More than one criterion may be used in a one single definition and following are examples of various definitions in some countries (NBE (2006)).

Table 2.1 SMEs Definition across Some Countries

Country	Enterprise Type	Workforce	Other Criteria
United States	Small	< 500	Annual Sales < US \$ 5 MM
European Union	Micro	< 10	
	Small	< 50	Annual Sales < 7 MM Euros or Assets < 5 MM Euros
	Medium	< 250	Annual Sales < 40 MM Euros or Assets < 27 MM Euros
Turkey	Micro	< 10	
	Small	< 49	
	Medium	< 199	
Thailand	Small	< 50	Assets < 50 MM bahts
	Medium	< 200	Assets < 200 MM bahts

Table 2.2 SMEs Definition in Egypt

Country	Enterprise Type	Workforce	Other Criteria
Egypt	Micro		Capital less than LE 50k
	Small	< 50	Capital between LE 50k - 1 MM

Table 2.2 shows that Egyptian 2004 Law No. 141 defined Small Enterprise as: Paid-up Capital lies between 50k Pounds to 1 Million Pounds and the number of employees should not be more than fifty; Micro Enterprises as: Paid-up Capital should be less than 50k Pounds.

2004 Law No 141 stated Social Fund for Development (SFD) as the key institution orchestrating the development of the sector by ensuring coordination between firms, ministries and various donor agencies. Specifically, the mandate of SFD was to provide micro and small enterprises with both technical and financial services to support their establishment, operation and growth (EL-Hawary (2007)), but there was more than one specific definition for SMEs in Egypt due to the varying approaches adopted by the planning, executive, statistical and financial sectors and entities.

Definitions of Financial, Non-Financial and Non-Bank Financial Services:

Financial Services: It simply means the Banking Sector Services provided to SMEs such as (1) Short Term Loans, compatible with SMEs business and income patterns; (2) Repeated Loans, where full repayment of one loan brings access to another and where the size of the loan depends on the client's cash flow; (3) Very small loans or bank overdraft facilities are also appropriate for meeting the day-to-day financial requirements of small businesses (Egyptian Banking Institute (2010)).

Non-Financial Services: The term refers to a range of government, intermediary and donor-supported non-financial services provided at various stages of development such as training, counseling and advise, information provision, technology development and transfer and business linkages (Abd-Elhamid (2007)).

Non-Bank Financial Services: NBFS are functioning like the way banks are functioning, though they

are different from banks on various counts. They are not authorized to accept demand deposits and are not a part of the payment and settlement system and as such, cannot issue cheques to their customers (Rabontu and Babucea (2014)). Some of these are discussed below:

1. Venture capital (VC) is provided by full-time, professional enterprises or private persons who invest both capital and management expertise in ambitious, fast-growing companies with the potential to develop into significant businesses. In addition to injecting cash into the business, the venture capitalist is likely to add considerably to the credibility of the company and to supply management expertise, support and access to contacts. As part of their mentoring and monitoring of their investment, they are likely to seek board membership (Egyptian Junior Business Association (2010); Giurca and Popa (2011)).

2. Leasing is a means of delivering finance, with leasing broadly defined as ‘a contract between two parties where one party (the lessor) provides an asset for usage to another party (the lessee) for a specified period of time, in return for specified payments’. Leasing is a medium-term financial instrument for the procurement of machinery, equipment, vehicles or properties (Fletcher et al (2005); Stojanovic and Guzovski (2013)). Some common forms of leasing are:

Financial leasing: It helps finance the eventual ownership of equipment, unless they have not fulfilled all payment of the contract period.

Operating Lease: In this case, the lessee doesn’t finance equipment purchase, but pays for a terminal use and maintenance of the asset again by installment amounts and since these are short term leases, the lessor will seek to, successively, loan out his asset (Scholz (2007)).

Hire Purchase: This is very similar to a financial lease in terms of operation. Payments are made at an agreed rate for an agreed duration, but the important differences are that ownership of the asset gradually passes to the customer with each lease payment.

Leverage Leasing: entails three parties where the lessor arranges to borrow part of the required funds, generally giving the lender the first mortgage on the asset. The lesser still receives the full amount on the investment tax credit (Muftahova, Nechaev and Antipina (2015)).

Sale and Lease Back: A sale and lease back takes place when a company sells an asset it owns to another firm and immediately leases it back (Amiri (2010)).

3. Factoring is a type of supplier financing in which firms sell their credit worthy accounts receivable at a discount and receive immediate cash. In addition, factoring is often done ‘without recourse’: the factor that purchases the receivables assumes the credit risk for the buyer’s ability to pay (Cucu (2013)) In this case, factoring is not a loan and there are no additional liabilities on the firm’s balance sheet although it provides working capital financing. Hence, factoring is a comprehensive financial service that includes credit protection, accounts receivable bookkeeping, collection services and financing (Klapper (2006)).

But a factor is a ‘person’ that purchases a debt for a discount owed to another in order to make a profit by collecting it. So, all factoring companies pay their clients for their invoices as they are issued. However, factoring companies also offer a range of professional services that might typically include: collecting payments from their customers, pursuing late payers, providing advice to clients on credit management, protecting the client against bad debts (Greater London Enterprise LTD (2003)).

4. SMEs Exchanges in order to increase access to equity finance for SMEs, a growing number of developing countries are creating specialized equity markets, differentiated from the main exchange. These new initiatives stem from the recognition that a specialized capital market segment called new markets can provide risk capital for promising entrepreneurs, promoting innovation crucial for sustainable economic growth (Chamber of India (2009)). New markets can be defined as regulated equity markets that focus on SMEs with high growth potential and set lower administration criteria.

2.2 Previous Studies about SMEs

Different studies about SMEs in Egypt were scanned, reviewed and analyzed to better understand the SMEs sector. The studies can be divided into three categories:

- Studies concerned with the competitiveness of SMEs
- Studies concerned with the role of non- financial sectors in supporting the SMEs
- Studies concerned with SMEs regulations

Studies concerned with the competitiveness of SMEs:

Macro level competitiveness is generated at the enterprises level. The Special interest shown by companies in their competitive assessment of the situation by referring to direct competitors makes it the most used level of analysis in literature. Tools that easily lends itself to comparisons between companies (benchmarking is one of the most used systems), particularity of the comparison, using quantitative indicators are widely accepted and easily comparable - the profit, market share etc. (Ceptureanu (2015)).

In a study by EL-Mahdi and Rashed (2006), which used the Egyptian Labor Market Panel Data 2006 to compare the changes that took place in the labor market, particularly the SMEs market,

from 1998 to 2006 in order to answer several questions, the most important questions are: How do the continuous economic changes affect the role of the private sector and distribution of workers among different sizes of enterprises? And are SMEs still the major job providers or are the medium and large sized companies starting to offer a growing percentage of work opportunities to the labor force? The study interpreted the figures and showed that the movement is happening in SMEs; huge numbers are leaving the market every-day and more are entering it daily, as new economic units are replacing marginal, inefficient SMEs all the time. But the study did not mention that the source of finance for SMEs may be responsible for their existence in the market. The current study will keep track of external sources of finance as a factor of SMEs performance.

In another publication by Maher (2007), the study used data on SMEs manufacturing sector and provided final recommendations to develop the small industries. However, the study did not mention any financing problems for SMEs and did not answer the question on how Egyptian SMEs can be competitive in the financing field. But the current study will use a case study (Nilex) and evaluate the companies' performance to explain what listed companies can gain from using NILEX debt or equity finance.

Another study presents an overview of the various technology support services provided by the SFD and programs to promote, develop and support SMEs as by EL-Gammal and Ashraf (2007), as the study explained that SFD is introduced followed by listing the main programs and organs inside SDF dedicated for provision of the technology support services. Each of these programs and organs responsible for providing of such services is summarized. But the study concerned only with the role of SFD in SMEs and did not cover the conceptual framework of financial and non-financial services. It did not presented regulatory framework for SFD scope of work as a governmental entity. The current study

explains both conceptual and organizational frameworks for NBFS.

Studies concerned with the role of non-bank financial services in supporting SMEs: Amiri (2010) examined the role of financial leasing companies in financing SMEs, and the study recommended that medium term financing for the purchase of capital should be available in developing countries. Leasing is more suitable for a developing nation's small and medium enterprises (SME) markets due to their weak collateral laws and the fact that the funds cannot be diverted for other efforts and then explained the challenges of leasing in Egypt.

The study; however, did not cover any legal framework of financial leasing in Egypt. Therefore, it did not address the scope of business of financial leasing companies in Egypt and did not assess the financial leasing. Nevertheless, it is an important study because it addresses the problems of financial leasing in Egypt. The current study uses the international experience to explain the application of leasing in SMEs. It lists all NBFS and the importance of using them in different project lifecycles.

There was a study presented by Ministry of Finance (2004), concerned with the application of Venture Capital (VC) application. It considered VC among the activities targeting and gearing towards finding solutions for the financial problems of SMEs. Venture Capital has a unique ability of combining both financial and business services into one model that reflects a direct response to the SMEs' needs. The study designed an action plan for VC services in Egypt. This was an important study since it used a methodology to assess the VC services and focused more on a legal framework for assessing VC services in Egypt without using data analysis. The current study will use a financial analysis to explain the role of NBFS in SMEs finance.

In another study introduced by USAID (2005), which is based on factoring as practiced internationally; it is an important study to recognize the legal and regulatory framework for factoring

in Egypt (definitions, requirements for a factoring Company, and requirements for a factoring contract). The study, however, did not use data or number of factoring companies in Egypt and did not explain how factoring as non-banking financial service is considered as a source of finance for any enterprise. The current study deals with factoring as a source of external finance for SMEs and how to apply the advantages of factoring on SMEs.

But the study prepared by Klapper (2006), discussed factoring as a non-banking financial service and its role in solving the access to finance problem. It discussed the advantages of factoring and its benefits for SMEs. It also discussed the disadvantages of using factoring as source of finance in the case of a weak contract, but the study did not deal with any data analysis. So the current study will use a certain criteria to assess the Egyptian NBFS.

And about the role of the Nile Stock Exchange in the development of Egyptian SMEs, Alasrag (2008) discussed the role of Nile Stock Exchange with its new listing rules and regulations that focus on a cost-effective regulatory regime adapted to achieve the needs and characteristics of SMEs. It explains how NILEX can solve the problem of access to finance in SMEs. Therefore, it is an important study to recognize the whole structure of NILEX. The study; however, did not analyze any of Nilex-listed companies. The current study; therefore, will provide answers to two questions. The first one is: How did Nilex increase the listed companies' performance? And the second question is: To what extent is Nilex's structure similar to the best international practices and experiences?

A recent study by Cerbusca (2015) highlights the problems faced by the SMEs in accessing adequate financing as one of the most significant barriers of the sector. Financial access is critical for SMEs' growth and development. The need depends on the stage of maturity and size of the enterprise. In order to facilitate the SME access to finance, it is necessary to adapt the best international practices and to adapt them at the local condition.

The study aimed at microfinancing as a tool to improve SMEs access to finance but failed to improvise on its applications. This study discusses NBFS as external source of finance for SMEs and explains the application of NBFS within SMEs.

And about SMEs access to finance, the Egyptian Junior Business Association (2010), designed a report to be a reference for small and medium companies on how to improve their access to finance. It provided information that clarifies and explains the different types of financing options now available in Egypt including financial and non-bank financial services. It also explained the types of financing tools to the needs of the companies at different points in time. The study aimed to provide details of requirements of the different types of institutions as prevailing in early 2010. It is considered as an overview study about external sources of finance for SMEs. But it did not provide any assessment analysis for any of these sources and did not refer to the regulatory framework of each source.

Studies on SMEs Regulations: The study presented by the Ministry of Finance (2007), to streamline the Egyptian laws, regulations and procedures governing property registration for SMEs. Moreover, that examines the role of the Egyptian regulations as legal constrains for SMEs during their lifecycle. The study provided recommendations to develop the legal framework by reforming the regulations of organization of government authorities, activities, registration fees, transparency, and Conciliation Property Taxation. It is a very important legal study for SMEs, but it did not use any financial analysis to determine to what extent the legal framework is considered as a main constrain for SMEs.

Almost all studies concerned with the competitiveness of SMEs have similar comments in SMES which is the lack of uniform definition of an M/SME that can be applied to Egyptian entities. It is therefore recommended to run a comprehensive survey in the region in order to ensure that a revised definition

captures the largest population of M/SME. Moreover, the studies concerned with NBFS have examined the services in supporting SMEs by similar criteria such as Regulatory framework and Standards of Establishing Companies and their activities. Hence, the current study will use the same criteria to assess the role in enhancing SMEs access to finance.

The studies concerned with Nilex are similar in common recommendations i.e. in order to increase listed companies in Nilex, there is a need to enhance the Awareness of investment in stock market and attract key players including high growth potential target SMEs and qualified sponsors/ advisors.

The previous studies which are concerned with SMEs or NBFS provided a clear methodology for assessment of the Egyptian NBFS by using a certain criteria such as Regulatory Framework (determine the regulatory body of NBFS), Standards of Establishing Companies (minimum capital requirements, scope of business), Current NBFS company's activities. But the current study is concerned with Egyptian NBFS and explains how SMEs can use those services in different project life cycle; moreover, that presents Nile stock exchange as a case study to explain how listing on Nilex affects the companies' performance.

3. METHODOLOGY

The primary goal of this study is to quantify the importance of NBFS within the SMEs sector in Egypt. NBFS in Egypt includes insurance, mortgage finance, financial leasing, factoring, venture capital and stock market. However, in relation to this study, the services that provide either debt or equity financing for SMEs will be selected which include financial leasing, factoring, venture capital and Nile Stock Exchange.

This study is modelled as deductive research using quantitative methods to analyze the role of Nilex in supporting SME and improving SMEs performance. It begins with calculating standard financial ratios using the financial statements of 16 listed companies in Nilex. The calculations look into cross-sectional

bases to compare the companies' performance with representative cooperative data. It also performs longitudinal analysis for financial statements of the oldest listed company (MASRIA CARDS) from year 2006 to year 2010 to compare company performance before and after listing in Nilex.

3.1 Research Analysis

Financial Analysis: Financial Statement of companies could be used to gauge companies' performance like Income Statement measures, company's financial performance over a specific period. Balance Sheet provides a detailed listing of company's assets and resources, and Statement of Cash Flows shows the resources of cash receipts and cash payments made by a company during an accounting period (CFA Institute (2011)). The financial ratios are usually based upon data taken from financial statements and are used to estimate company's risk, assign rating to company's bonds and predict a company's chances of insolvency (USDA (2010)). This study uses financial analysis to analyze 16 listed companies in Nilex performance and calculate financial ratios delivered from the companies' financial report. The financial analysis process includes the following phases:

Determine Purpose and Context of Analysis: The main purpose is to examine the performance of listed companies in Nilex to know how the listing in SMEs exchange affects the companies' performance. And this analysis will be through cross-sectional analysis for all listed companies in year-end 2009.

Collect Input Data: The relevant financial data collected is financial statements for the companies published through Nilex and GAFI for all 16 listed companies and time series financial statement for the oldest listed company MASRIA CARDS from the year 2006 to 2010.

Process Input Data: The calculated financial ratios is conceded as the main output from financial statement. A

Financial Statements Program, designed by GAFI through IT sector depending on standard Egyptian accounting principles, was used in data processing.

Perform a Follow-up of Financial Analysis: The standard ratios used in this study to examine the companies' performance are divided into 3 categories: Liquidity Ratios: it measures the companies' ability to pay its short term financial obligations such as current and quick ratio cooperative ability to meet short term obligations (USDA (2010)). The second category is Solvency Ratios: it measures the companies' ability to satisfy long term obligation including the company's financial leverage (CFA Institute (2011)). The third category is the Profitability Ratios: it measures the management's effectiveness at generating earning from revenues or involved capital or assets such as Return on Equity (ROE) which measures the rate of return on the ownership interest (shareholders' equity) of the common stock owners and Return on Assets which measures the productivity of assets regardless of how these assets are financed (USDA (2010)).

Evaluation Analysis Approach: Evaluation analysis explains the nature and main characteristics of both NBFS and SMEs. In addition, the study highlights different obstacles and problems at the levels of SMEs and NBFS and builds a matrix for all these issues and action taken towards them.

The criteria used here are: Regulatory Framework for NBFS which is very important to develop each service by determining potential regulatory body; Standards for Establishing Companies like deciding the criteria for determining who can perform NBFS activities; Current Non-Bank financial Companies' Activities: number of companies, scope of business etc.; and Government support: could take different forms such as developing suitable tax systems.

Case Study Analysis: Nilex is considered as first step for Egypt in using non-bank financial institution for SMEs finance and on the other hand using stock exchange as an external source of finance. The study also tries to explain Nile's relaxed listing roles and how it helps the company in the listing and offering process. Nilex is the first SMEs stock market in the MENA reign, following extensive researches and studies on similar international markets, which succeeded in helping small companies expanding their business.

3.2 Data Collection Sources

Both primary and secondary data was used. Primary Data includes calculated financial ratios for Nilex listed companies by using balance sheet program developed in GAFI in order to know the company performance. Secondary Data includes numerical data defined as following:

- No of Egyptian SMEs, count of workforce and paid capital
- No of Leasing Established Companies during period (2000 - 2010)
- No of Factoring Companies during period (2000 - 2010)
- No of Venture Capital Companies during period (2000 - 2010)
- Balance Sheet and Income Statements for listed companies in Nilex
- No of established companies considered as SMEs during the period (2000-2010)

3.3 Population

Only 16 companies were listed on Nilex as of Dec 2010 and this study tries to examine the role of Nilex in enhancing the companies' performance for all of these companies. Census technique was used to list all the elements in the population to measures their performance. The study unit of analysis is whole population which is 16 companies.

Since the elements are considered as a single member of the population, this study uses a purposive example i.e. Masria Card Company to explain how this company has been affected by listing in Nilex by showing its performance before and after listing. This is the oldest Company listed in Nilex. The company had a Paid-up Capital of about 10.8 MM with largest no of shares, approx. 2.1 MM in year 2009.

Table 3.1 Population size of the research

No	Company name	No	Company name
1	Misr Intercontinental for Granite & Marble (Egy-Ston)	9	AL Moasher for Programming and Information Dissemination
2	Sanabel Co. Lo. T.T	10	International Company for Fertilizers and Chemicals
3	Ferchem Misr Co. for Fertilizers & Chemicals	11	Ameco Medical Industries
4	Pharaoh Tech for Control and Communication Systems	12	Kato Agriculture Development Co.
5	Misr Kuwait Investment & Trading Co	13	El-Barbary Investment Group
6	Rabya – landscaping	14	Utopia
7	Intergroup Egyptian International Group for Construction, Agriculture & Real Estate Development	15	El Bader Plastic
8	Al Oroba trading mining and supplying	16	Masria Card

3.4 Data Analysis

Cross-sectional analysis for calculating financial ratios of all listed companies was used because the listed companies did not apply for listing in Nilex in the same year. The analysis aims to interpret the performance of listed companies and to explain how listing in Nilex affected the risk and profitability of companies by comparing between old and new listed companies. On the other side, the longitudinal analysis of Masria Card Company in time period of 5 years (2006-2010) was used to explain the changes in company's performance before and after listing in Nilex.

4. ASSESSMENT FOR EGYPTIAN NON-BANK FINANCIAL SERVICES

In most countries, SMEs have great difficulty in obtaining the necessary financial resources to effectively scale up and grow their businesses. Access to traditional growth capital, including debt and equity, is often prohibitively costly because of insufficient legal and regulatory policies and inadequate financial markets. On the other hand, some countries recognize that well-developed NBFS can provide external finance and help improve the risk and maturity profile of corporations' external financing.

4.1 General Features of Egyptian SMEs

Basic laws organizing Egyptian SMEs: In 2004, a new SMEs law 'Small Enterprise Development Law No. 141' was decreed with main objective to provide support to SMEs by defining and describing the main incentives provided by the law. In 2005, a new Tax Law No. 91/ 2004 was decreed according to which tax rates were reduced from around 41% to 20%. The income brackets were widened and the tax exemption was increased. The new tax law was associated with several incentives for enterprises (EL-Mahdi and Rashed (2007)). The basic rights for Egyptian SMEs according to the SMEs law are as follows:

- 10% of vacant land available for investment in the industrial and tourist zones new urban communities and reclaimed lands are allocated to SMEs
- The project owner shall pay 1% of the projects paid up capital with a maximum of L.E. 500 for small projects and L.E. 200 for micro projects on the account of services provided by all governmental bodies (EL-Hawary (2007))
- Stands allocated by different areas for displaying products of small and micro enterprises shall be offered at 50% discount of the rental fees
- Enterprises may not be closed except in case of a violation, which shall necessitate that a permanent committee headed by a judge and comprising representatives of the Chamber

of Commerce and the SFD shall be formed by virtue of the competent governor's decree to review the complaints regarding such closure decisions. Settlement of disputes arising between the enterprises and other bodies, with which it deals, shall fall within the functions of such committee (Economic Bulletin (2006))

The Economic Significance of SMEs Development: SMEs account for over 90% of active enterprises in Egypt and contribute to over 80% of GDP and 75% of total employment (Thiemann and Arlet (2010)). The SFD has succeeded in providing 1MM job opportunities in such enterprises since its establishment in 1991 until the end of 2003 (Economic Bulletin (2006)). Omran (2007) points out that the number of small enterprises of more than 128,000 contributes with 19% of employment and medium enterprises, more than 40,000 contribute with 10% of employment. Over 70% of SMEs operate in the trade sector, followed by services and manufacturing sectors. Table 4.1 shows the number of SMEs establishments according to the Central Agency for Public Mobilization and Statistics data in 2006.

Table 4.1 Operating Establishments of SMEs (excluding government) - By size & No. of workers

No. of Workers	1-to-4	5-to-9	10-to-99	100-999	1000+	Total
No. of Establishments	2,252,550	152,445	42,538	3,163	207	2,450,903
% out of Total Establishments	91.90%	6.20%	1.73%	0.12%	0.00%	
No. of Workers	4,242,805	911,253	914,256	762,698	423,021	7,254,033
% out of Total Workers	58.50%	12.60%	12.60%	10.50%	5.80%	

The above table shows the number of establishments employing less than 10 workers represents 98.1% of total operating establishments (excluding government) in Egypt, which

are considered micro enterprises. The number of workers employed by establishments employing less than 100 workers is 6,068,314 accounting for 83.65% of total employment by operating establishments (excluding government), which are considered micro and medium companies. So, in order to trace the number of establishments in time serious, the next chart explains the number of SMEs establishments from year 2000 and 2010 according to GAFI statistics data depending on the companies' establishment according to Law 8 / 1997 and Law 159 / 1981 as follows:

Chart 4.1 SMEs Establishment (2000-2010)

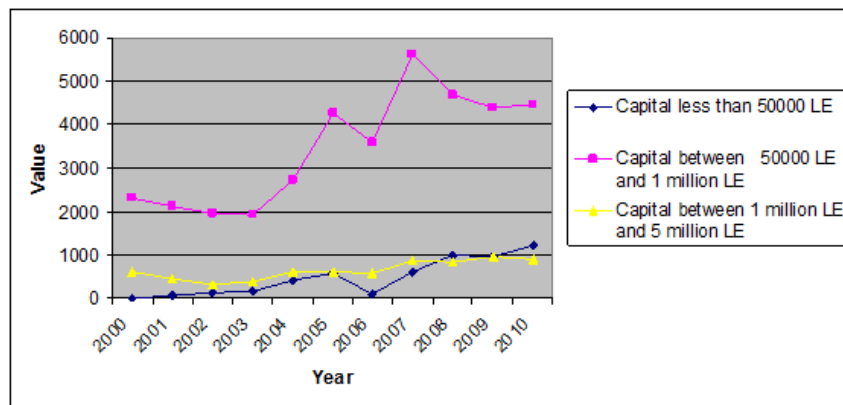


Chart 4.1 shows that the line presenting the medium enterprises (capital between L.E 50000 and L.E 1 Million) is the heights line which means that the medium enterprises represent the largest number of companies' establishment with the total number of 38,041 companies in years from 2000 to 2010, followed by small enterprises with total number of 7,153 companies and then micro enterprises with 5,222 companies. The main difference between the two results is that the data collected by CAPMAS included the enterprises, which have been established in SDF. So, the largest number was for micro enterprises, but GAFI data

depended only on companies that have been established under the law No 8/1997 and the law No159/ 1981.

Constraints of SMEs in Egypt: The vast majority of SMEs is far from meeting the competitiveness standard and is facing increasingly hostile conditions. New trade agreements are being signed by Egypt that will make markets, locally and internationally, more open and competitive. While these provide new opportunities, unless SMEs increase their competitiveness, they will not be able to survive this new competition. Plus, access to finance problems and legal constraints is faced by SMEs.

Competitiveness Constraints: Thiemann and Arlet (2010) explained that there is a policy gap as regards SMEs with high-growth potential; sector institutions are active but work in isolation from each other and are sometimes ill-equipped to meet need of fast growing SMEs. The institutional setting of SME policy is complex, encompassing a range of ministries and specialized agencies. Ambiguities in the delegation of responsibility and task assignment pose a risk of policy gaps, overlaps and duplications of policy measures.

High Number of Informal Business in SME Sector: distorts competition and inhibits the effectiveness of government policies, according to OECD study in 2010, enterprises that operate informally constitute nearly 40% of the total.

Limited, Non-structured and Uncoordinated Marketing Channels: Most SMEs rely on direct sales to customers in local markets. The 2006 data about SMEs suggests that the chief source of demand for more than 90% of SMEs is direct sales to consumers. This is confirmed by findings of SFD Mapping Survey that the vast majority of enterprises rely on direct sales, irrespective of the enterprise size as Table 4.2 shows, this marketing pattern results in intermittent production patterns that

disable MSEs from utilizing scale economies. It is estimated that 56% of all MSE production is done on demand, with 44% done on a continuous basis (Social Fund for Development (2007)).

Table 4.2 Marketing Channels (in %) by Size Category

Size of Enterprise	Means of Reaching Customers		
	Direct Sales	Dealers & Distributors	Other
Micro	93.60	6.10	0.30
Small	93.10	6.90	0.00
Total	93.60	6.20	0.20

Table 4.2 indicates that SMEs lack the skills, education and often the linguistic abilities to tap into sources of market information and are unlikely to invest in conducting market research or hire marketing professionals or join distribution networks.

Legal Constraints: Excessive regulation can be harmful to the competitiveness of any economy, its growth and prosperity. It is most harmful to the development and growth of the SME sector due to the high cost of compliance in terms of time, money and lack of transparency causing confusion and uncertainty. Regulation is not costless. Yet, there is generally a lack of recognition on the part of the regulators of the negative effect of the regulatory burden on the development, productivity and competitiveness of the SME sector (EL-Hawary (2007)).

Financial Constraints: Limited access to finance and the absence of financial services specifically tailored to the needs of SMEs have inhibited their growth in Egypt. According to survey conducted by NILEX, SMEs account for only 10% of total capital accumulation in Egypt and while 75% OF SMEs apply for banking loans, 92% of applications are rejected. The result is that loans to SMEs

account for only 6% of the total loan portfolio of Egyptian banks (Thiemann and Arlet (2010)).

SMEs have failed to attract the interest of financial institutions as the latter are tilted toward large companies. The Egyptian financial system has suffered from significant entry and exit barriers; as a result of which competition was limited and inefficient banks were allowed to continue operating. The prevailing legal framework in Egypt still constrains the cost and terms of finance. Some laws are poorly written, especially those regarding secured transactions, bankruptcy and settlement of disputes (Nasr (2007)).

The Chart 4.2 shows Leading Constraint to Egyptian Manufacturing Firms (by size). As mentioned in ICA report (2009). Egypt Small Formal Manufacturing Enterprises are more likely to identify themselves as seriously constrained by a number of factors ranging from informal competition to tax rates to the cost of and access to finance.

Chart 4.2 Leading Constraints to Egyptian Manufacturing Firms

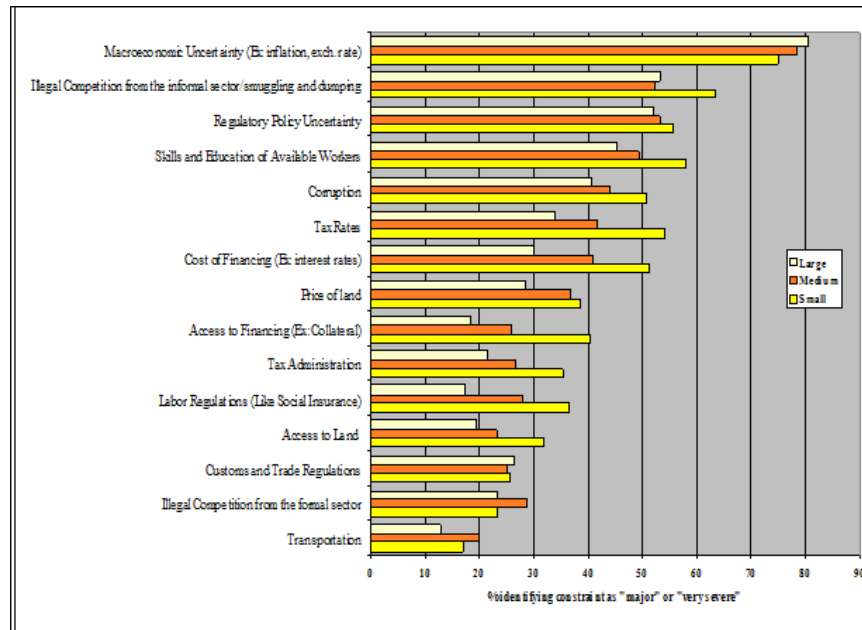


Chart 4.2 shows that the medium-sized manufacturers are more constrained than large firms by factors like tax rates, cost of financing, price of land, access to financing and labor regulation. Small service sector firms do not show this pattern of being more constrained, perhaps indicating lesser scale economies to dealing with the investment climate in services sectors than in manufacturing. Medium-sized service firms do stand out from small and large ones in terms of their identification of worker skills and education and of corruption as serious constraints.

4.2 The role of NBFS in Supporting SMEs

Application of Venture Capital within SMEs: VC can be an important source of external finance for SMEs, particularly for high potential start-ups, high growth businesses known as 'gazelles' and in the case of family firm succession. However, it should be emphasized that VC accounts for only a relatively small proportion of external finance for SMEs (Arjan et al. (2009)). VC operations

follow a cycle that starts from fund raising and ends with the exit of the fund from a specific investment (Dutta (2005)). The main components of this cycle are as follows:

- **Fund Raising:** Venture capital funds starts with a venture capital firm that seeks capital to initiate the fund. Professionally managed venture capital firms are generally private partnerships or closely held corporations funded by private and public pension funds (Dutta (2005))

- **Fund Management:** The quality of fund management is the most crucial factor for a fund's performance. Project management skills are required to manage at all levels of a business to meet business performance measures and enable tactical flexibility and control (Dutta (2005))

- **Investment Strategies:** Venture capitalists can be generalist or specialist depending on their investment strategies. They can be generalists, investing in different industries, different geographic locations and/or different business stages (Dutta (2005))

- **Deal Identification & Due Diligence:** Before performing any in-depth analysis of the deals, the venture capitalists carry out an initial screening that would focus on evaluating some of the project's aspects (Dutt (2005))

- **Value Adding:** The role of VC does not stop after the investment is made; rather the skills of the capitalist are most required after the investment is in place. The role of VC includes providing strategic advice and the ongoing monitoring of the project (Ministry of Finance (2004))

But the most important disadvantages of venture capital is that smaller firms will be the most affected by the higher fees financiers charge for use of small amount of money as banking loans so many SMEs do not prefer this type of finance (EL-Gawaga (2007)).

Application of Leasing within SMEs: In most developing countries leasing may be the only form of medium-to-long-term

financing available for purchase of equipment that can expand production levels or increase productivity of workers, arranged more quickly and simply than conventional bank loans because additional security often does not need to be established. Satisfactory understanding of rights and obligations under a lease contract can serve to minimize or eliminate adverse decrease in service or resale value of leased equipment arising from deficient maintenance activities (Muftahova, Nechaev and Antipina (2015)).

The SMEs sector is not monolithic and can be categorized into different layers, for example, the financial assistance for SMEs in the lowest layer (Startup Phase) need access to working capital to finance purchases of supplies. They also need materials and the financing services appropriate to their needs. Their repayment capabilities will be characterized by short cycles of repeated loan drawdown and repayment. The enterprises in this lowest layer of SME will not be suitable candidates for lease financing. SMEs in middle and upper phases (Operational Phase) require financing for the acquisition of additional tools and equipment to support growth and expansion of their production. Therefore, SMEs will benefit most from the expanded access to financing that leasing provides (Gallardo (2000)).

Scholz (2007) remarks a number of disadvantages of using leasing in financing SMEs. For example, leasing of highly specialist equipment may also pose difficulties because the secondary market may be particularly thin and may be unsuitable for micro enterprises and the risk of an individual lease one of the disadvantages of using leasing for SMEs finance (legal risk, market risk).

Application of Factoring within SMEs: It is argued that factoring is a highly appropriate source of working capital finance for smaller businesses as there are rational reasons to use factoring within SMEs financing such as: the availability of funds through factors is higher to smaller 'growing' businesses than traditional sources (i.e. bank overdrafts) because factors consider the sales

invoice as a secure asset, whereas banks typically look for fixed assets as security.

SMEs are not fully familiar with the techniques of financing through factoring. Some of these organizations do not accept to resort to factoring in their aversion to any form of debt without having to address rigorously the opinions. Another category of SMEs refuses to resort to factoring for lack of knowledge-but not to recognize their lack of information, while other traders believe the Bank reduce the profit without having to take the risk of the business (Cucu (2013)).

Factors are able to process and pay against invoices considerably more quickly than the time taken to renegotiate any overdraft extension. The credit management services offered by factors often provide an economic solution to smaller businesses, which either doesn't pose the relevant skills internally or the opportunity cost of undertaking these functions is prohibitive. Factoring is an alternative route by which a business can increase its cash flow to fund expansions (Greater London Enterprise LTD (2003)).

Role of SMEs Exchanges in Supporting SMEs: New markets that function well offer a range of benefits: greater access to growth capital for innovative SMEs, new jobs through entrepreneurship, more investment opportunities for domestic portfolio investors and local venture capitalists, new sources of revenue for local stock exchanges and an expanded mechanism for recycling public funds to promote SMEs (Yoo (2009)). SMEs exchange has the following features to achieve their role in SMEs finance:

- Size: All the new markets are significantly smaller in size than the main market
- Access: to new markets can be measured by the amount of equity offerings and number of listed firms

- Liquidity: because they deal with small capitalization firms, naturally do not have the same market liquidity and depth as main market (Yoo (2009))
- Market Dynamics: SMEs exchange is a high entry and exit rate, reflecting their focus on high-growth SMEs (Omran (2009))
- Lower Costs for Listed Firms: firms are invariably wary of the costs of going (and remaining) public. These costs, both direct and indirect, range from listing fees to insurance for independent directors (Omran (2009))
- Support Services for Issuers: in several countries the new market and the government provide services aimed at nurturing young enterprises that are or will be listed on the market such as promoting institutional investment, boosting the visibility of listed firms, and raising public awareness of alternative investments (World Bank (2007))

4.3 International Experience Overview in Using NBFS in Supporting SMEs

Venture Capital: The developed countries were the pioneers in establishing a successful and effective VC market that could incorporate the SMEs sector and allow for its growth and development and both US and UK stand as the most two active VC markets in the world. The experiences of US, UK, Germany, Thailand, India, Mexico and Argentina were reviewed presenting a sample that included pioneers; such as US and UK, failure experience that turned into success as that of Germany's, and developing countries with some similarities in economies; such as India, Thailand, Mexico and Argentina (Ministry of Finance (2004)).

The main requirements for creating a VC climate as specified by Hellman and Puri (2002) are to link the international experience to the climate success factors and ensure the importance and weight of these factors when initiating a VC industry. It is an investment tool that invests in high risk businesses

in expectation of high return. In Europe (2007), the venture capitalists associated with European Venture Capital Association had about 5,300 investments in 3,290 SMEs (up to 200 employees) with a total amount of € 6.6 billion. The average investment amounted to € 1.2 million. The share of SMEs in the total investments is about 55% (Arjan et .al (2009)).

Financial Leasing: In the first phase of leasing in Europe, many small leasing companies were founded. The focus of these companies lay in the covering of regional markets and companies, but in the 70's leasing could be strengthened in the market. Between 1970 and 1980 the leasing business in Germany increased by 800% (regarding the new leasing volume).

Particularly, by the increasing activities of the banks in context of their subsidiaries and participations, the leasing business received new impulses, generally it applies today that leasing companies are quite considered as innovative and partly also as trendsetters on the capital goods markets (OECD (2009)). The product leasing itself did not change fundamentally in the last years - the structure of the customers and their surrounding legal, economic and competition environments changed a lot. These new surrounding conditions must be optimally used under integration of the capital market. This is the really large challenge for the leasing industry during the next years (Scholz (2007)).

Factoring: Factoring is continuously gaining importance in Europe. About 1000 companies currently offer factoring services throughout the world; 435 of which were situated in Europe in 2001. Europe counts for 66% of the worlds' factoring market. Between 1996 and 2001 the factoring turnover has risen in Europe, reaching € 474 billion purchased debt in 2001 (an increase of 15% compared to 2000). This kind of development can be observed in all Member States with the exception of Sweden and France, where a decrease of about 35% and 76%, respectively, was achieved between 1996 and 2001. The highest increases of factoring turnover can be seen in Spain (+300%) and Greece (+547%). In Spain, factoring was, at least indirectly,

promoted by legal changes (Austrian Institute for SME Research (2003)).

About 11% of SMEs in Europe use factoring, but considerable differences can be observed between countries. Whereas SMEs in France, for example, are using factoring (32% of them take advantage of it), it is hardly ever used in Sweden (3%). Factoring is specifically targeted at and suitable for smaller enterprises. On average, 50% of the total number of European factoring companies' clients has an annual turnover of less than € 2 million, 81% of less than € 5 million and 91% of less than € 15 million (Austrian Institute for SME Research (2003)). As factoring is a relatively new financing instrument, up to now, the penetration rate of 11% is rather low (Austrian Institute for SME Research (2003)).

SMEs Exchange: There are three high-growth SMEs' markets in Europe: Alternative Investment Market (AIM), European Association of Securities Dealers Automated Quotations (Easdaq) and the Euro.NM network.

AIM was launched in June 1995 and is operated by the LSE. It is a second tier market, replacing the Unlisted Securities Market (USM), which opened in 1987 providing an alternative market for the younger and smaller companies, and closed in 1996. However, the management of AIM is completely autonomous from the Official List and has its own regulation (Giorgino and Magnani).

Easdaq was launched in November 1996. It was created by venture capitalists, investment bankers, securities dealers and investment institutions to service a need in Europe, to support economic development and innovation in up and coming young, innovative and high-tech companies, experiencing growth and looking for financing.

Euro.NM was set up in March 1996 in the legal form of a European Economic Interest Group. It is designed to build a decentralized European stock market, based on a network of similar national markets. It is a very flexible organization with the

task of defining the minimum requirements necessary to link these new markets according to the principles of subsidiary (Giorgino and Magnani).

The markets are evolving to represent different companies by size, sector, growth etc. and are acquiring their own unique character (Elnagar (2001)). The major differences can be perceived between the three markets, as far as number of listed companies. AIM, the oldest of the markets, has the largest number of companies with over 300. Easdaq whose strategy is to attract somewhat larger companies, has been growing gradually since its launch, while Euro.NM has shown a persistent increase with a recent strong upward trend (Commission of European communities (1996)).

4.4 Egyptian Non-Bank Financial Services

Organizational Framework of Egyptian Non-Bank Financial Services: Law No. 10 of Year 2009 regulating the non-banking financial markets and instruments established the Egyptian Financial Supervisory Authority (EFSA). The Authority supervises instruments like Capital Markets, Derivative markets on Financials and Commodities, Insurance activities, Mortgage Finance, Financial Leasing, Factoring and Securitization.

EFSA shall replace the Egyptian Insurance Supervisory Authority, the Capital Market Authority and the Mortgage Finance Authority in enforcing the provisions of the Insurance Supervision and Control Law No.92 of year 1981, the Capital Market Law No.95 of year 1992, the Depository and Central Registry Law No. 93 of year 2000, the Mortgage Finance Law No. 148 of year 2001, as well as any other related laws and decrees that are part of the mandates of the above authorities. The Authority shall be considered the competent administrative body entitled to enforce the financial leasing provisions promulgated by Law No.95 of 1995 (Law No. 10 of year 2009).

The new SME Market, NILEX, which is the first small & medium cap market in the MENA region, was launched in October

25th, 2007 as a separate entity within the Cairo & Alexandria Stock Exchange (CASE) framework and was launched to improve SMEs' access to finance (World Bank (2008)).

Assessment Criteria for Egyptian Non-Bank Financial Services:

Venture Capital Assessment

Regulatory Framework: VC activity in Egypt was recently introduced and regulated under the Capital Market Law No. 92/1995. It is also covered by the Investment Guarantees and Incentives Law No. 8/1997, as one of the activities allowed for under this law. EFSA is a regulator body for VC according to law 10/ 2009. Moreover that Article No. 123 of the Executive Regulations of the Capital Market Law issued under the Ministerial Decree No. 135/1993 defines venture capital activities.

Venture Capital Activities in Egypt: Venture Capital companies must take the form of a joint stock company or a partnership limited by shares; the capital of which may not be less than LE 10 million, to be paid in full upon formation (Ministry of Finance (2004)). The total number of venture capital companies in Egypt is nine companies according to data of companies' establishment (GAFI (2010)). This number of companies is still a small number, which highlighted that the VC industry in Egypt is still immature. A small percentage of them are not operating as VC companies. EL-Hawary (2008) pointed that the reasons behind the existence of non-operating companies are the shortage of skills & experience to manage VC Funds and absence of key players in the PE market: Angel Investors, Sponsored Advisors – Market still underdeveloped.

Leasing Assessment

Regulatory Framework: The leasing industry was established in Egypt by Law No. 95 of year 1995 governing the financial leasing companies with further Amendments in late 2003. Amendments allow the leasing of all assets, including cars that were not permitted under the previous law and land as long as it is attached to a productive activity. Soroor (2007) pointed out that Law No. 8 of 1997 governing investment and its amendment by Law No. 13 of 2004 gave a 5-year tax exemption for leasing companies. The Income tax law cancelled all these tax exemptions and allowed a 50% tax reduction for companies established before June 2005.

Standards for Establishing Companies: The Financial Leasing law No. 95 of year 1995 and its amendments by law No. 16 of year 2001 impose that the ownership of financial leasing companies should be financial companies (limited liabilities, joint stock company or a partnership limited by shares with LE 500000 as a minimum capital requirement (law no 16 of year 2001).

Current Leasing Companies' Activities: According to the Ministry of Investment's reports, the total numbers of Egyptian leasing companies is 268 companies (Ministry of Investment (2010)) and the total number of deleted companies is 61 companies. So, the total active number of Egyptian leasing companies is 208 companies.

Chart 4.3 Total number of contract and the value of contracts

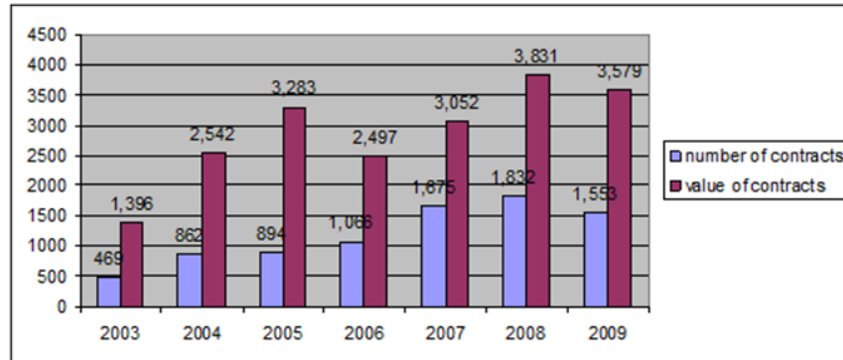


Chart 4.3 shows that the total number of contracts in 2009 are 1553 with value 3579 EGP as the rate of leasing activities growth of the value of the contracts increased by about 2% in 2009 although the number of the contracts increased by 2%. Moreover, the total accumulated number of contracts is 8230 with LE 2000 million. So, it is discernable from the analysis that there is a good potential for the involvement of the leasing companies in providing their services to the SME sector in Egypt. But SMEs' awareness of leasing activities in Egypt was not very remarkable, as almost a lot of the SME were not even aware of the existence of leasing companies in Egypt (Amiri (2010)).

Factoring Assessment:

Regulatory Framework: Factoring is governed by the regulatory body EFSA according to law No. 10 of Year 2009 on Regulating Non-banking Financial Markets and Instruments (Article II). Decree No. 120 of the year 2010 was issued by the EFSA's BOD governing the factoring companies and the rules and documents needed for factorizing companies. The Prime Minister's decrees covering

factoring in Egypt were as follows: Article (1) of the Executive Regulations of the Investment Law No. 8 of year 1997 issued by Prime Ministerial Decree No. 1247 of 2004 provides a definition of factoring, factoring contracts and factoring services as set forth in the Executive Regulations of the law (USAID (2005)).

Standards for Establishing Companies: EFSA Board of Directors degree No. 120 of year 2010 imposes that the ownership of factoring companies should be joint stock companies with business being limited to factoring as a commercial company or a bank, with sufficient capital and with the needed commercial and financial know-how, should be able to engage in factoring as a specific business and division within its larger (USAID (2005)) and the company could add other filed of business after EFSA approval. The paid-in capital is not less than LE 5 million or equivalent amount in foreign currencies (EFSA, Decree No. 129 of year 2010).

Current factoring Companies' Activities: Enterprises finance their accounts receivables through banks or from their own sources, increasing their financing requirements. Like other non-bank financial institutions, factoring companies do not have access to potential clients' creditworthiness information and are impeded by the inefficient legal mechanism for collection of receivables. But the first factoring company establishment in Egypt was in July 2009 with participations of CIB and FIM in Malta and the International Finance Corporation (IFC) and the total number of factoring companies establishment is three companies (GAFI (2005))

4.5 SME Finance Needed at Different Stages in SME Lifecycle

The SME life cycle includes 3 life stages. These include the initial start-up phase, the early development phase and the growth and maturity phase. SME financing needs vary depending on a number of variables including the stage of development of a business, its growth objectives, the sector in which the firm operates, and management attitudes towards risk (European Communities (2009)). Table 4.4 shows the type of finance required in SMEs lifecycle as follows:

Table 4.4 Type of finance required in SMEs lifecycle

Phase in SME Lifecycle	Type of financing required
Seed stage	Informal equity and loans from founder and associates, Bank loan if available and needed
Start-up stage	Informal equity and loans from founder and associates and contacts, Bank loan if available, Leasing for equipment
Expansion stage	Equity from original sources, plus trade investments or venture capital, Loans from bank, Other sources of finance including leasing and factoring, Retained profits
Replacement Capital	Trade investment, venture capital or IPO

SMEs could be financed from a variety of sources. An easy distinction can be made between 'internal' and 'external' financing sources. Internal financing includes owner investment, funding through retained profits and sale of assets whereas External Financing includes Debt Finance, Leasing and Hire Purchase, Factoring, Trade Credit, Venture Capital etc. The source of finance most appropriate to fund SME growth and development varies according to the stage of development of the firm. To conclude the states of Egyptian NBFS, Table 4.5 shows the performances of NBFS (VC, Leasing, factoring) according to pervious criteria.

Table 4.5 Egyptian Non-Bank Financial Services

Criteria	Venture Capital	Financial Leasing	Factoring
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Regulator Body	EFSA	EFSA	EFSA
Regulation framework	Law No. 92/1995 Law No. 8/1997 Law No. 10/2009	Law No. 95/1995	Law No. 8/1997 Law No. 10/2009
Business scope of work	Joint Stock Company or partnership limited by shares	Joint Stock Company or partnership limited by shares	Joint Stock Company or a partnership limited by shares, limited liabilities
Minimum capital requirement	LE 5 million	LE 500000	LE 10 million
Government Support	√	√	√
Number of companies	9	268	1

4.6 Summary

Egyptian SMEs have a great participation in GDP and employment as SMEs accounts for more than 85% of establishment but Egyptian SMEs still suffer from obstacles, (competitiveness, legal and access to finance). The access to finance problem could be solved by enhancing suitable NBFS, but depending on NBFS as external source of finance related to the phase in SME lifecycle and depending on how those services are developed to serve SMEs.

In Egypt NBFS are still have unremarkable role in SMEs finance and the main reasons for this is the weak limited and poorly available information on potential clients and borrowers. In addition, a number of specific regulations impede the development of the various non-bank financial services and institutions, and still others need to be put in place to facilitate it. So, Egypt has to increase the awareness of using NBFS, and enhancing the companies by generating incentives for them.

5. EMPIRICAL ANALYSIS FOR THE ROLE OF NILE STOCK EXCHANGE IN SMEs FINANCE

NILEX is the first market for SMEs' stocks in the Middle East and North Africa. It is an initiative to provide cheap funding for promising SMEs in order to raise capital and expand their activities without complex procedures and without the need for guarantees or assets (Omran (2009)). In World Bank study on 'Access to Finance and Economic Growth in Egypt' stated that although there are more than 24 SME markets around the world, only a few are successful. These include AIM in UK, TSX-venture in Canada, and KOSDAQ in Korea. The existence of a special market for SMEs is therefore not a guarantee for access to equity finance for SMEs (Nasr (2007)). To study the role of Nilex in Egypt, the model of AIM in the UK would be taken in consideration to know to what extent the Egyptian model is close and similar to successful models. The role of Nilex in enhancing the SMEs performance was studied by calculating the financial ratios of financial statements of listed companies.

5.1 Theoretical Framework of Nile Stock Exchange

Issues for Possible Regulatory Framework: Several decrees were issued to organize the operations of NILEX. These include Ministerial Decree No. 259/2007 issued to determine listing fees in NILEX. As NILEX is a market in the Egyptian Exchange (EGX) for growing medium and small size enterprises, legal decrees were issued by the Chairman of the Capital Market Authority (CMA) to control NILEX as follows: Decree No. 62 of 2007 added to the rules of listing and delisting of securities in the Stock Exchange issued pursuant to CMA's BOD Resolution No. 30 of 2002. The decree is related to the rules regulating the listing of securities issued by SMEs as article No. 1 explains, that SMEs shall be listed on the Stock Exchange tables which have issued capital of not less than EGP 25 million, and the amendments to this decree by the Egyptian Financial Supervisory Authority BOD

decree No. 74 of year 2010 to increase minimum capital requirement for NILEX companies to EGP 50 million. Decree No. 63 of 2007 defines the rules regulating trading, clearing, and settlement in the SMEs Market. Decree No.64 of 2007 regulates the work of accredited SMEs sponsors.

The same organizational structure was found in AIM (UK), which is a sub-market of the LSE, allowing smaller companies to float shares with a more flexible regulatory system than is applicable to the main market (LSE (2010)).

Capital Requirement of Listing Companies: It should be noted that the minimum capital of a company to be registered on NILEX is EGP 500 thousand and the maximum is EGP 25 million, while the required minimum in the main stock market is EGP 20 million, and companies with less capital are to adjust during the transition period, but this does not mean that they will degraded directly to the NILEX; they only must reapply to it (Omran (2009)) and the applicant company must have a nominated advisor approved by the CMA. The nominated advisor advises and assists the company on all its responsibilities during the application process and ensures the company's compliance to the listing and disclosure rules. The nominated advisor's obligations and responsibilities will be maintained for at least two years from the listing date (Alasrag (2008)). The total number of Nominated Advisors approved by CMA is 30 advisors.

Also AIM has certain capital criteria as the company seeking admission to AIM should be a UK company and must be pupil limited company in order to be able to offer its shares to the public. In order to do business, the nominal value of shares must not be less than 50000 Euro or 25% of the nominal value of shares and any premium must be wholly paid (LSE (2008)). Moreover, in order to be eligible for AIM, an applicant must appoint a nominated adviser and an AIM company must retain a nominated adviser at all times (LSE (2010)).

Listing Rules: Medium and Small Companies that qualify to be listed on Nilex should fulfill the following rules (NILEX (2010)):

- All listed securities must be deposited at the Central Depository.
- Company's by-laws should not include any constraints on the trading of the securities to be listed.
- Company must have financial statements for at least one fiscal year preceding the listing application.
- The issued capital should be fully paid at a par value ranging from EGP 1 to EGP 5 per share.
- The number of issued shares to be listed should not be less than 100 thousand shares.
- Shareholders' equity shouldn't be less than 50% of Company's Paid Capital in the year preceding the listing application.
- The minimum free float should be at least 10% of the total issued shares and the number of shareholders should not be less than 25 (Alasrag (2008)).

The AIM's listing rules are different from the Egyptian Nilex's rules, as AIM has fewer limitations, for example no minimum shares should be in public hand and no minimum market capitalization (LSE (2010)). In addition to the previous requirements, both exchanges are similar in the issuance of Annual accounts as the listed companies should submit their quarterly and semi-annual financial statements, approved by the company's management, within 45 day from the end of the period and should submit their audited annual financial statements within 90 day from the end of fiscal year of the financial statement. And the exchange will publish the companies' financial statements and financial results for only one day on the trading terminals.

5.2 Companies Activities

Number of Companies Listed in Nilex: In Egypt, 16 companies has been listed on Nilex. As shown in Table 5.1, the listed companies differ from each other in its date of listing and their Issued paid-up capital.

Table 5.1 Companies listed on Nilex with their Issued Paid-up Capital

No	Company name	Listing Date	Issued paid-up capital	Listed Shares
1	Misr Intercontinental for Granite & Marble (Egy-Ston)	15/9/2010	8,650,000	8,650,000
2	Sanabel Co. Lo. T.T	15/9/2010	30,000,000	15,000,000
3	Ferchem Misr Co. for Fertilizers & Chemicals	15/9/2010	30,000,000	15,000,000
4	Pharaoh Tech for Control and Communication Systems	21/7/2010	5,000,000	1,000,000
5	Misr Kuwait Investment & Trading Co	21/7/2010	20,000,000	20,000,000
6	Rabya – landscaping	14/07/2010	7,000,000	1,400,000
7	Intergroup Egyptian International Group for Construction, Agriculture & Real Estate Development	16/06/2010	10,000,000	10,000,000
8	Al Oroba trading mining and supplying	10/3/2010	3,000,000	1,500,000
9	AL Moasher for Programming and Information Dissemination	10/2/2010	7,073,000	7,073,000
10	International Company for Fertilizers and Chemicals	13/01/2010	20,000,000	10,000,000
11	Ameco Medical Industries	24/12/2009	16,500,000	3,300,000
12	Kato Agriculture Development Co .	16/12/2009	12,000,000	2,400,000
13	El-Barbary Investment Group	15/10/2009	10,000,000	10,000,000
14	Utopia	15/10/2009	5,000,000	1,000,000
15	El Bader Plastic	11/6/2008	1,700,000	1,700,000
16	Masria Card	11/6/2008	10,795,930	2,159,186

Table 5.1 shows that the oldest two companies have been listed on Nilex in 2008 are El Bader Plastic and Masria Card and there are 4 companies have been listed in 2009 and in 2010 increased by 10 companies. It is considered that the first trading section which was in June 2010 may be the reason for increasing the number of listed companies by 10 companies in 2010. Also the International Company for Fertilizers and Chemicals and Sanabel Co, have the largest issued paid-up capital (EGP 30,000,000) with 15000000 listed shares.

On the other hand, AIM is the world's leading market for smaller, growing companies – and key to its success is a balanced regulatory environment, specifically designed to make the process of going public as smooth as possible for smaller companies. As a result, over 2,800 companies have joined AIM since the market's launch in 1995, raising more than £49 billion (LSE (2010)). But this is not a comparison between two markets as the Egyptian Exchange launched the first trading session in the Nile Stock Exchange (NILEX) on Thursday 3 June 2010. So Egypt is actually starting using the mechanism of SMEs stock market.

Table 5.2 Results of the First Trading Section in Nilex

Company Name	Par Value	Closing Price	Value LE	Volume	Market Capitalization
Al Bader Plastic	1	8.76	2,628,000	300,000	15
Barbary Investment Group	1	7.00	7,000,000	1,000,000	70
UTOPIA	5	52.00	522,600	10,050	52
Al Moasher for Programming and Information Dissemination	1	6.10	305,000	50,000	43

Table 5.2 shows that 4 companies were traded during the first trading session, recording a total trading volume of 1.4 million shares worth LE 10 million. The shares' prices registered

significant increases in the first trading session compared to their par value. Barbary Investment Group (BIG) ranked first in terms of value traded, recording LE 7 million, followed by El Bader Plastic, registering a trading value of LE 6 million. Utopia recorded more than LE 500 thousand and AL Moasher recorded a trading value of more than LE 300 thousand (Nilex (2010)).

Benefits given to SMEs when joining NILEX:

- **Relaxed Listing Requirements:** Nilex offers more flexible listing rules compared to the main market with respect to the minimum capital, number of shareholders and number of shares to be offered to the public as well as the company's financial track record.
- **Lighter, yet Cohesive Disclosure Rules:** SMEs, have to submit their audited annual financials to the exchange and the Capital Market Authority, while quarterly and semi-annual financials are to be approved by the company's management only before submission (Elserafy (2009)).
- **Lower Listing and Trading Fees:** The annual listing fees levied on medium and small enterprises are reduced to 0.5 per thousand of the capital with a minimum of EGP 500 and a maximum of EGP30,000 (Ministerial Decree No. 259/2007).

Table 5.3 shows a comparison between bank loans and stock market in financing SMEs using some criteria as financing cost and potential to increase fund and efficiency of companies (Alasrag (2008)).

Table 5.3 Comparison between Banks Loans and Stock Market

No	Criteria	Bank loans	Stock market
1	Cost of Finance	High	Low
2	Maximum Fund Level	There is maximum level to finance SMEs; It is related to the company capital	There is no limits for finance
3	Increasing Fund	Limited and according to bank conditions	More flexible
4	Technical Support	There is no technical support	There is a technical support through nominated advisor
5	Company Performance	There is no effect on company performance	The credibility rules enhancing the company performance

5.3 Performance of Nilex-Listed Companies

Financial Analysis for Listed Companies on Nilex: The main objective of this part is to know how listing in Nilex can affect companies' performance and the current study uses the financial ratios calculated from financial statements to measure aspects of companies' performance. Following ratios are used:

- Current Ratio = Current Assets/Current Liabilities
- Financial Leverages = Average Total Assets / Average Total Equity
- Debt to Equity = Total (Interest-Bearing) Debt/ Total Shareholders' Equity
- Return on Assets = Net Income / Average Total Assets
- Return on Equity = Net Income / Average Total Equity
- Return on Sales = Net Profit / Sales

Table 5.4 shows the ratios calculated from financial statement. Current Ratio is considered as measuring of a short term debt paying ability and provides a good measure of liquidity. The newer companies listed in Nilex have higher risk because they still have higher assets than their liabilities. And these ratios are going down when the companies are being older.

Table 5.4 Risk Ratios for Companies listed on Nilex

No	Company Name	Listing Date	Current Ratio	Debt to Equity	Leverages
1	Misr Intercontinental for Granite & Marble (Egy-Ston)	15/9/2010	3.20	0.00	14.54
2	Sanabel Co. Lo. T.T	15/9/2010	1.64	0.00	2.76
3	Ferchem Misr Co. for Fertilizers & Chemicals	15/9/2010	2.22	0.00	17.40
4	Pharaoh Tech for Control and Communication Systems	21/7/2010	1.45	0.00	2.54
5	Misr Kuwait Investment & Trading Co	21/7/2010	7.20	0.00	1.90
6	Rabya - landscaping	14/07/2010	4.42	0.00	1.27
7	Intergroup Egyptian International Group for Construction, Agriculture & Real Estate Development	16/06/2010	0.41	0.00	1.33
8	Al Oroba trading mining and supplying	10/3/2010	4.20	0.00	4.90
9	AL Moasher for Programming and Information Dissemination	10/2/2010	0.45	0.00	2.66
10	International Company for Fertilizers and Chemicals	13/01/2010	1.24	1.33	1.26
11	Ameco Medical Industries	24/12/2009	5.36	0.00	21.22
12	Kato Agriculture Development Co .	16/12/2009	0.14	0.00	2.80
13	El-Barbary Investment Group	15/10/2009	6.30	0.00	11.24
14	Utopia	15/10/2009	7.40	0.00	1.13
15	El Bader Plastic	11/6/2008	1.72	1.70	4.83
16	Masria Card	11/6/2008	1.29	0.14	2.32

The older listed companies in Nilex such as 2 companies listed in 2008 (Masria Card & El Bader Plastic) has more liabilities so their current ratio tends to be smaller which means more risk for those companies. There is an obvious increase in

debt to equity ratio in old companies (Masria card & El Bader Plastic) than the majority of other newer listed companies which have 0 debt to equity ratio. As the increase in debt to equity ratio means increasing in shareholder equity and increasing in company debt which means higher risk for the company. So it could be conclude that being listed in Nilex affect the company risk by increasing it through increasing its debt and company liabilities, so it is very important to evaluate the same companies profitability to compare between their risk and profitability so the next table presents calculated profitability ratios for the same companies.

Table 5.5 Profitability Ratios for Companies listed on Nilex

No	Company Name	Return on Assets	Return on Equity	Return on Sales
1	Misr Intercontinental for Granite & Marble (Egy-Ston)	0.03	0.04	0.35
2	Sanabel Co. Lo. T.T	0.07	0.11	0.12
3	Ferchem Misr Co. for Fertilizers & Chemicals	0.05	0.07	0.09
4	Pharaoh Tech for Control and Communication Systems	0.06	0.10	0.40
5	Misr Kuwait Investment & Trading Co	0.00	0.01	0.03
6	Rabya - landscaping	0.05	0.06	0.07
7	Intergroup Egyptian International Group for Construction, Agriculture & Real Estate Development	0.01	0.05	0.20
8	Al Oroba trading mining and supplying	1.30	1.29	0.37
9	AL Moasher for Programming and Information Dissemination	0.00	0.00	0.00
10	International Company for Fertilizers and Chemicals	0.01	.005	0.01
11	Ameco Medical Industries	0.15	0.16	0.18
12	Kato Agriculture Development Co.	0.03	0.04	0.09
13	El-Barbary Investment Group	0.14	0.15	0.06
14	Utopia	0.00	0.00	0.00
15	El Bader Plastic	0.30	0.39	0.33

16	Masria Card	0.22	0.43	0.27
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Table 5.5 show profitability ratios for 16 companies listed on Nilex using their financial statements in 31/9/2009. Using this cross sectional analysis and comparing between old and new companies listed in Nilex the study presents the following empirical analysis:

- There are 2 companies listed on Nilex in 2008, 4 in 2009 and 10 in 2010. In general the oldest companies listed have more profitability ratios then newer companies which mean increasing in their net profit than the other companies.

- The greater profitability ratios are for the first 2 listed companies which presents retune on assets, equity, sales as follows (Masria card - 0.22, 0.43, 0.27 & El Bader Plastic-0.3, 0.39, 0.33).

- In 2009 the Nilex did not begin to trade yet, so just listing in Nilex enhancing the companies' performance.

Financial analysis for listed companies on Nilex: As mentioned in research methodology the study presents Masria Card Company as example to know how Nilex is affect the performance of companies.

Company Profile: A pioneer and market leader, Misr Security Systems (MSS) has foreseen the Smart Technology wave from very early stages. It is the most established industry leader in Egypt and the Middle East. In 1985, the card division of MSS was created to be the first local PVC cards manufacturing facility in the region. During this period, this card division introduced the first ATM card, membership card, health insurance card and scratch off cards. After many years of success, the card division separated to become Masria Card, an independent state of the art smart card manufacturer and total solutions provider.

Date of Listing on Nilex	11/6/2008
Issued Paid-up Capital	EGP 10,795,930
No of Shares	2,159,186

Par Value of each Share	EGP 5
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Table 5.6 Financial Ratios for Masria Card Company

Year	Current Ratio	Debt to Equity	Return on Assets	Return on Equity
2006	0.52	0	0.02	0.04
2007	0.61	0	0.01	0.02
2008	0.66	0	0.02	0.03
2009	1.5	0.14	0.22	0.38
2010*	1.7	0.16	0.66	0.59

Table 5.6 selected the profitability ratios and risk ratios to explain how Nilex affects the performance of the oldest company. It is clear that there is a positive relation between risk and profit as there is an increase in risk as current ratio increased from 0.52 in 2006 to be 1.7 in 2010 and Debt to Equity increased from 0 to be 0.16 in 2010, and increase in profitability by as ROA raised from 0.02 in 2006 to be 0.66 in 2010 and ROE from 0.04 in 2006 to be 0.59.

Hence, listing on Nilex affects the companies' performance through increasing their net income and their profitability ratios, with increasing their risk which interprets some number of companies listing on Nile stock exchange through previous 3 years. GOE has to develop safety roles for those companies to protect both listed companies and investors.

The SMEs can be benefit from Nilex through relaxed listing requirements, lighter, yet cohesive disclosure rules, lower listing and trading fess. Although there are good rules, listing in Nilex is still very limited and this is may be attributed to many reasons such as weak awareness, high risk and the absence of skilled management. So, the government of Egypt has to take procedures to protect both listed companies and investors; the government has to increase the awareness of investors to invest in Nilex and offer training programs for listed companies to know

how to use trading mechanism in an effective way to increase their profit and decrease their risk.

6. CONCLUSION & RECOMMENDATIONS

SMEs are vital in promoting economic growth, competitiveness, entrepreneurship, innovation and in creating new jobs. Ensuring adequate access to finance so that SMEs can grow and achieve their full potential is central to achieving the objectives of the renewed Lisbon partnership for growth and jobs. So, many SMEs, especially fast-growing firms, will need 'external' sources of finance, but the relative importance of different types of external financing for SMEs, and the extent to which this is required, differs according to SMEs lifecycle.

NBFS can serve as external source of finance for SMEs and are regulated by the Egyptian Financial Supervisory Authority according to Law No. 10 of year 2009. The study explains the application of NBFS within SMEs by assessment criteria such as issues for a Possible Regulatory Framework, standards for establishment and companies' activities. Moreover, the study presents the Nile Stock Exchange as a case study of non-bank financial institutions that support SMEs and evaluates the listed companies using cross sectional analysis and calculating their financial ratio.

Results are presented as follows:

- There are more than one governmental entity dealing with SMES.
- NBFS are not yet well developed in Egypt because of reasons like large role of the state in financial intermediation-through ownership and tightly prescribed, weak limited and poorly available information on potential clients and borrowers. In addition, a number of specific regulations impede the development of the various non-bank financial services and institutions.
- There is no awareness of using NBFS as an alternative source of finance.

- There is a good potential for the involvement of the NBFS especially leasing companies in providing their services to the SME sector in Egypt. But still, there are some companies which are worried about the high risk that can be involved in SME financing.

- There is absence of skilled and qualified fund management to secure the implementation of successful investment plans.

- Although Nilex is considered as an initiative to provide cheap funding and flexible listing rules, there are only 16 companies listed in 3 years; this is due to high risk, and absence of (incentives of those companies, awareness, and skilled management). These factors are responsible for the less number of companies that get listed on Nilex.

- Although Nilex is similar to other SMEs stock exchanges in the trading mechanism, there is absence for high controlled procedures to protect investors.

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