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Analyzing the Investment Decision and Financing Method of the French Small and Medium-Sized Enterprises

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Abstract : SMEs are always considered as a national priority due to their contribution to job creation, innovation and growth. Once the start-up phase is crossed with encouraging results, the company enters the phase of growth. In order to improve its competitiveness, maintain and increase its market share, the company is in the necessity even the obligation to develop its tangible and intangible investments. SMEs are generally closed companies with special and critical financial situation, limited resources and difficulty to access the capital markets; their shareholders are always living in a conflict between their independence and their need to increase capital that leads to the entry of new shareholder. The capital structure was always considered the core of research in corporate finance; moreover, the financial crisis and its repercussions on the credit's availability, especially for SMEs make SME financing a hot topic. On the other hand, financial theories do not provide answers to capital structure's questions; they offer tools and mode of financing that are more accessible to larger companies. Yet, SME's capital structure can't be independent of their governance structure. The classic financial theory supposes independence between the investment decision and the financing decision. Thus, investment determines the volume of funding, but not the split between internal or external funds. In this context, we find interesting to study the hypothesis that SMEs respond positively to the financial theories applied to large firms and to check if they are constrained by conventional solutions used by large companies. In this context, this research focuses on the analysis of the resource's structure of SME in parallel with their investments' structure, in order to highlight a link between their assets and liabilities structure. We founded our conceptual model based on two main theoretical frameworks: the Pecking order theory, and the Trade Off theory taking into consideration the SME's characteristics. Our data were generated from DIANE database. Five hypotheses were tested via a panel regression to understand the type of dependence between the financing methods of 3,244 French SMEs and the development of their investment over a period of 10 years (2007-2016). The results show dependence between equity and internal financing in case of intangible investments development. Moreover, this type of business is constraint to financial debts since the guarantees provided are not sufficient to meet the banks' requirements. However, for tangible investments development, SMEs count sequentially on internal financing, bank borrowing, and new shares issuance or hybrid financing. This is compliant to the Pecking Order Theory. We, therefore, conclude that unlisted SMEs incur more financial debts to finance their tangible investments more than their intangible. However, they always prefer internal financing as a first choice. This seems to be confirmed by the assumption that the profitability of the company is negatively related to the increase of the financial debt. Thus, the Pecking Order Theory predictions seem to be the most plausible. Consequently, SMEs primarily rely on self-financing and then go, into debt as a priority to finance their financial deficit.

Keywords : capital structure, investments, life cycle, pecking order theory, trade off theory
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