Influence of Internet Finance on SME Financing — A Case Study of P2P Model

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Abstract. The development of internet finance provides some ways for SMEs to solve financing difficulties. Although the internet financing model has unique advantages, it also positively and adversely influences SMEs. In order to capitalize on internet finance to solve financing difficulties, SMEs have to reinforce system construction and enhance their competitiveness, and the national applicable laws, regulations and rules should be issued to create a good Internet financing environment.

Introduction

Along with the accelerated process of global economic integration and the good development of Chinese economy, SMEs have been growing in terms of number and scale. According to “Analysis Report of In-depth Market survey and Investment Strategy of Chinese Business Operation Projects 2017-2022”, there are 40,000,000 SMEs in China, which account for 99% and contribute to 60% GDP, 50% taxes and 80% urban employment. However, the failure of SMEs to address the financing difficulties is considered as a big obstacle that restricts our economic development. Exploration and financial innovation are efficient alternatives to ease the financing difficulties of SMEs.

P2P (peer to peer) finance, also referred to as P2P lending, is one of the internet finance models and refers to small-sum lending transaction between individuals. The continuous progress and invention efforts of internet economy, and the active P2P model and the participation of large e-commerce operations provide SMEs with a new financing channel, which in turn has eased their financing pressure to some extent. According to the data of WDZJ.Com, as of the end of May 2016, China had 4,080 P2P online lending platforms, with the accumulated trading volume of RMB 2,036.135 billion. The flexible and convenient trading experience it delivers has greatly lowered the threshold of financial services and improved financial inclusion, thus providing SMEs with a new financing channel and option[1].

Internet Financing Models and Advantages

Internet Financing Models

P2P. P2P financial model is also known as “peer-to-peer lending” or “point-to-point” model, the specific way of operation is that an individual who needs to borrow money can directly post his borrowing need on P2P platform, provider can also find his customer check his credit information and repayment capacity on the platform, both sides can sign a contract on their own accord, provider can provide the money in need. P2P is a new lending model with more simplified procedure and faster process than bank loan, making it easier to lend and borrow small-sum money if needed. Provider can find the individual who needs money, thus exploiting his funds in a better way.

Crowdfunding. Crowdfunding, also known as public funding, is a behavior of raising funds for the proposed project or product on the crowdfunding platform. Under the crowdfunding model, an investor will make a decision on investment according to the information posted on platform and
his own will, and fundraiser can raise funds through this model. Crowdfunding is a new fundraising method and an important measure of raising funds for hi-tech industries. The advantages of crowdfunding include low threshold, ease of operation and fund security, so that it has been gradually accepted by the marketplace.

**E-commerce Finance.** E-commerce finance is an e-commerce platform-based activity that is conducted by enterprises, operator can obtain the actual operating condition and sales performance concerning the platform-based enterprises, and get a general idea about the enterprise or individual who applies for financial services through basic analysis of big data, before deciding whether to release financing loans to enterprise or individual. E-commerce finance reduces the risk arising out of information asymmetry when the internet finance institution examines and approves the credit loans. It is specifically targeted and can effectively mitigate extremely high risks, so as to reduce bad debts of enterprises.

**Internet Financing Advantages**

**Functional Advantages.** Internet financing model functions as a platform where all customers who have an access to internet and mobile network can make payment, conduct wealth management, transfer money from time to time and from place to place, thus evolving the transaction process; it has a financing function that allows lender and borrower to conduct free transactions on the internet finance platform, which not only meets the borrower’s capital demand but also fulfill the investor’s investment intention; it also has a payment function ensuring that all money transactions between borrower and lender are completed by a third party, which secures the mutual transactions, protects the safety of their funds, simplifies the transaction process, and makes the transactions convenient.

**Cost Advantage.** Under the internet finance model, borrower and lender directly conduct transactions on the platform, which not only effectively reduces the transaction cost, but also allows for more convenient operation. The information of both sides can be fully disclosed according to the information collected and the analysis of big data on the platform, so that the mutual trust will be enhanced to ensure the smooth transactions. Internet finance saves the intermediary cost of traditional finance industry by relying on the analysis of big data, leading to reduced transaction cost. Internet finance integrates material flow, information flow, and capital flow to effectively control cost and create cost advantage.

**Effects of Internet Finance on SME Financing**

**Positive Effect of Internet Finance on SME Financing**

The emergence of P2P means a new trial for SME financing, investor and financier can cross over the space and time limitations, conduct communications and interactions on the internet platform from time to time and from place to place, exchange information in a quicker and better way.
way, and facilitate the process of concluding deals. The biggest advantage of P2P is to allow borrower and lender to make deals on the internet platform, rather than rely on the traditional financial institution, which helps SMEs a lot in raising funds. In this way, SMEs not only break down the procedural restrictions they had before by exploiting the internet strengths, but also cross over the limitations of commercial bank loans on SMEs, matching capital needs responded. The P2P model is as shown in Fig.1.

**Internet Finance Develops New Financing Channels.** Internet finance has gradually diversified the financing channels of SMEs. Individuals can raise funds through crowdfunding, P2P and other web-based channels, and the “open access” of such platforms has liberated businesses and customers from the space and time limitations. P2P is mainly serving the SMEs, crosses over the limitations of commercial bank loans on SMEs, provides them with a lot of helps, and effectively addresses the narrow financing channel. In addition, internet finance also plays a crucial role in addressing the high risk of SME financing, the efforts it makes in analysis of big data can clearly identify the intensity of such risk, and its development is opening up new financing channels for SMEs.

**Internet Finance Eases the Financing Pressure on SMEs.** The emergence and development of P2P enable banks and financial institutions to clearly understand the borrower’s credit status and risk exposure, reduce the cost and time in investigating banks and financial institutions, allow borrowers to raise financing funds efficiently and quickly, and solve shortage of funds in due time. Moreover, internet finance can deliver a huge amount of financing funds that cannot be achieved by traditional financial model, which not only meets the financing needs of SMEs, but also greatly eases the financial pressure on SMEs.

**Internet Finance Reduces Financing Cost.** The development of internet finance has also reduced the financing cost of SMEs to some extent. Internet finance in turn enables SMEs and financial institutions to conduct better communications, visually presents the borrower’s needs to financial institutions through analysis of big data and processing of internet technology, allowing financial institutions to drastically reduce the cost in acquiring and processing information. Several main modes of internet finance have developed rapidly in the internet finance market, meet the capital needs of lender and borrower through internet platform, allowing for the evolution of financial method from low efficiency and high cost to high efficiency and low cost.

**Adverse Effect of Internet Finance on SME Financing**

Internet finance mainly challenges the SME financing by increasing their financing risks, and the financing risks it creates include credit risk, legal risk and security risk.

**Credit risk.** For example, P2P is a small-sum loan specifically provided to SMEs, but has a low threshold, lacks of government supervision, and high risk of default. At present, the domestic P2P industry uses an appropriate guarantee measure for business development, but this still cannot avoid credit risk effectively.

**Legal risk.** Currently, Chinese legal system on the protection and regulation of internet financial operations has not been well-established, and the daily operations of P2P platforms are not constrained by applicable laws and regulations, which provides loopholes for financial fraud and illegal fundraising. Moreover, no applicable laws and regulations are provided to punish those individuals who fail to repay P2P loans on schedule.

**Security risk.** The security of P2P is the problem that internet finance must face. The rapid development of P2P has exposed the technical security issues. The hacking of customer information on P2P platform through remote attack or virus implantation causes unnecessary losses to customers.

**Feasible Strategies of Improving SME Financing under the Internet Finance Model**

**Improve the Internet Financing Environment**

To improve the internet financing environment, firstly, we should strengthen the supervision on
internet finance. Currently, Chinese legal system on the protection and regulation of internet financial operations are quite deficient, the daily operations of P2P are not constrained by applicable laws and regulations, and internet finance is often beyond the range of financial supervision. In this concern, we should establish applicable laws and regulations, and build a stringent financial supervision system to improve the internet financing environment. Secondly, we should control the risk of P2P. Risk control is the priority for traditional financial model and internet finance, we should proactively create a good credit atmosphere, establish internet financing platforms with credit assurance, assess the risk factor of individual platforms, establish and improve the risk triggering mechanism, and ensure the capital security of investor and lender. Lastly, we’d better make the internet finance innovative. The first alternative is to classify different business products for different customers by making business products innovative, especially to improve credit business; the second alternative is to make channel business innovative, because the convenient internet financial channel will ease the financing of SMEs; the third alternative is to seek efficient service modes, show more concerns on customer needs, tailor more professional services, and effectively combine online and offline services, so that the service efficiency will be improved in a better way.

**SMEs should Seek Self-improvement and Growth**

Under the internet finance model, the process of solving the financing issues faced by SMEs will be facilitated by improving their financial environment, but the underlying measure is to seek self-improvement and growth.

On the one hand, SMEs should transform their operating mechanisms. In the internet finance market with intensified competition, SMEs can also enhance their development capabilities and market competitiveness by improving the internal management structure, introducing talents and technologies, and strengthening the brand building, so as to boost the confidence of investors. Moreover, they should make profit models more innovative, enhance core competitiveness, and increase their appeals to internet financing as far as possible.

On the other hand, SMEs should maintain a good credit standing. In the context of internet finance development, the emergence of P2P and crowdfunding and other internet financing models is partially because that traditional financial institution makes too strict requirements for financing subjects, but SMEs are often disqualified for credit conditions. However, as the development of internet finance tends to be more standardized, internet financing will attach more importance to customer credit conditions. As a result, enterprise should adhere to the principle of honesty and integrity, and increase its credit rating and level, so as to get the trust from banks, financial institutions and other fund providers.

**Conclusion**

SME financing is a big problem all over the world, but the role that internet finance plays in SME financing is being recognized by the society. Although internet finance has some technical and regulatory deficiencies, it has unique advantages. P2P has played an extremely important role in helping SMEs in expanding the financing channel and reducing the financing cost. Of course, it also exposes certain risks and problems as an emerging financing model. However, with the continued attention paid by the state government to internet finance, and the improvement of internet finance supervision system, it is justified to believe that internet finance will better serve SME financing services in future and effectively solve its financing difficulties.

**References**


