The proximity law of small business finance

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"A small business is not a little big business" This is almost certainly the most commonly quoted sentence in introductory chapters to books and articles on the management of SMEs. Over time, the postulate of the SME as an entity governed by specific laws of management has established itself as a genuine paradigm structuring research in the field (Torrès and Julien, 2005), giving legitimacy to the creation of scientific journals and research associations like the ICSB (*International Council for Small Business*) in the English-speaking world or the AIREPME (*Association Internationale de Recherche en Entrepreneuriat et PME*, International Association for Research in Entrepreneurship and SMEs) in French-speaking countries.

This theory of the specificity of SMEs has now been widely accepted. It nevertheless has one major drawback. It does not precisely define the specificity of SMEs. If SMEs are specific, it must also be admitted that large companies are, too. Using the same term, *specificity*, to define two such fundamentally different realities is clearly unsatisfactory. The two types of specificity thus need to be qualified and given a more precise term.

The theory that we put forward is that the specificity of the management of SMEs is proximity. Proximity refers to the classic concepts of family[1], friendship and neighbours, as well as to more modern concepts such as "link" and "social capital". All these concepts have the particularity of revealing a great importance for the small business.

Taking the "proximity" factor into account when discussing the management of SMEs is part of a broader research trend that grants greater importance to relational aspects than to transactional aspects. It is precisely the importance and quality of these relations that are one of the key points of the analysis of the specificities of SMEs. Fuller (2003) even states that relations and personalisation are at the very heart of the specificity of the management of SMEs. "Small businesses embody the personalities of their owners, and their ways of doing business with stakeholders are largely personal. The human "touch" and personal networks create the opportunity for enterprises with little market or financial power to stay more in control of their future" (Fuller, 2003). These remarks coincide with those made by Gibb (1997: 18), "The very essence of small company management is the personal day-to-day handling of transactional and other relationships with networks of customers, suppliers, bankers, accountants, solicitors, agents, marketing channels, workers and regulatory authorities as well as (more intimately) acquaintances, friends and family" (Gibb, 1997: 18).

The aim of this article is first to propose a reformulation of the concept of SME and to show to what extent proximity can be considered as the federating element behind the specificity of the management of SMEs. Secondly, we will show how proximity can also qualify finance in SMEs.

1. SME like a proximity management model

To highlight the central role of proximity in managing SMEs, we will use the concept of SME formulated by Julien (1982 [with Chicha]; 1990; 1998)[2]. This concept

[1] It should be noted that originally the word proximity, from the Latin *proximitas* and *proximus*, was used in the 15th and 16th centuries in its legal meaning of family relations in deeds of inheritance (Le Boulch, 2001).

[2] According to Boissin, Castagnos and Guieu (2000), who have conducted a detailed bibliometric study on works devoted to the subject of SMEs for the period 1990-1995 into the French-speaking area, one very clear result is that scientific production is concentrated on the dominant authors and centres. The most notable result, beyond the number of articles published, is that Pierre André Julien is one of the most often cited authors (with Michel Marchesnay), making this author the central pivot in a network on the specificity of SMEs.

is characterised by small size, 1) centralised management, 2) a low level of labour specialisation, 3) simple, informal and direct internal and external information systems and 4) intuitive, implicit and short-term strategy. We will demonstrate to what extent each of these specificities of SME management can be analysed as a particular form of proximity.

1. 1. From centralised management to hierarchical proximity

The management style of an SME is highly centralised, sometimes exclusively concentrated on the person of the company owner-director, to such an extent that in opposition to the hyperfirm, which defines an extremely large multinational company, we can propose the term "*Ego*firm" to define a small, or very small, business. Although it is generally admitted that the level of centralisation depends on the size of the company, on the character of the director and on the value of his subordinates, it also depends on the conditions of the company. The considerable centralisation of the owner-director's power can be effective only under conditions of great proximity and within the framework of a compact structure. It is because he is in close contact with his employees that the owner-director increases his hierarchical domination. The influence of the owner-director on his company depends on his omnipresence. "As it is uncommon for a small company to have several geographically dispersed sites, the owner-director can be personally acquainted with almost every employee and is able to assess his or her qualities. Moreover, he is personally known to all of them" (Barreyre, 1967). The small dimension of SMEs thus facilitates the multiplication of direct, personal contact and a management style often directed towards tasks and people. "Better integration such as this leads to a personal valorisation for individuals and, in cases where the owner-director is the mainspring of this valorisation, centralisation will be more than accepted: it will be wished for." (Gervais, 1978).

Ultimately, the high level of centralisation of SME management styles, as well as the weakness of their hierarchical structure, are features which can only be enhanced in a context of proximity. Proximity increases centralisation and lessens interest in creating intermediaries. This phenomenon of intensification of the centralisation of SMEs can be interpreted as a form of *hierarchical proximity*.

1. 2. From a low level of specialisation to functional proximity

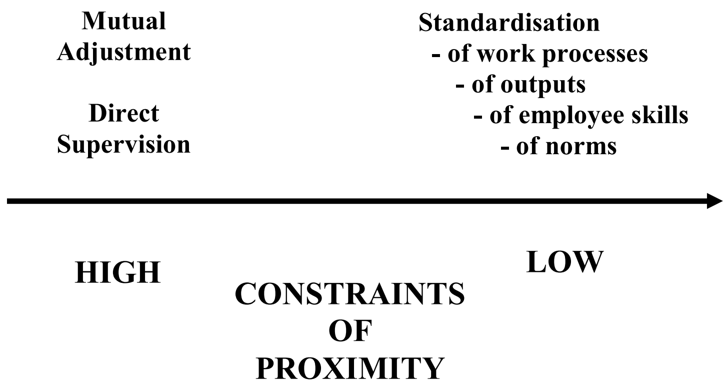
According to Capet, Causse and Meunier (1986), “in small companies, the division of work is not very intensive. Only a few services or functions are concerned. Many tasks are performed by the owner-director, who not only manages, but also plays the role of service manager, and even carries out tasks himself”. SMEs can be considered as “a whole, where all the functions are integrated or at least very highly connected, and where the owner-director controls every aspect, managing several functions and taking part personally in some of them” (Julien and Marchesnay, 1992). Generally, small companies seem to have a low level of specialisation. “At the decisional level, there is considerable interweaving between the decisions of finalisation (strategic), animation (administrative) and exploitation (operational). Here again, we can speak of a low level of specialisation, with the owner-director occupying the roles of composer, conductor and sometimes even performer” (Marchesnay, 1991). SME management is based above all on the versatility of its employees.

This versatility can only be used if the owner-director and members of the company are permanently in touch with the various problems arising in their organisation. Here also, proximity between the players makes versatility possible, turning all concerned into permanent observers of the various problems faced by the other members of the company. Sales staff are closer to the factory workers and operatives. These numerous, and repeated, contacts lead to better awareness and understanding of the various problems faced by the company. Proximity stimulates versatility and, as a result, discourages task separation within the company.

Similarly, the intensity of the constraints of proximity differ according to the coordination mechanisms implemented by the organisation. Proximity modifies both the nature of organisation relations and the efficiency of coordination modes. By taking up

Mintzberg's typology of coordination mechanisms (1989) and looking at them from our viewpoint, that is, integrating the notion of proximity into the understanding of organisations, it can be considered that mutual adjustment and direct supervision are the modes that are the most sensitive to proximity, unlike others which make distance management and coordination easier, such as standardisation of work processes, outputs, employee skills and norms.

Figure 1. Mintzberg's coordination mechanism and proximity constraints



(*source: Torrès, 2000*)

It can nevertheless be seen that SMEs are generally characterised by coordination mechanisms that are highly constrained by proximity. The small size of the businesses makes it pointless turning to standardised mechanisms. Given that SMEs are generally characterised by a compact structure, it can also be considered, however, that this characteristic favours the implementation of proximity-based coordination mechanisms. If internal communication is barely formalised and most often verbal, this is because the proximity conditions required for this type of communication are effective. Once again, proximity appears as the mechanism that explains the coordination modes that are specific to SMEs and that define their framework of validity.

Finally, if SMEs are a management model with little structure, this is because they correspond to a compact spatial configuration. Low levels of task specialisation are highly conditioned by a context of proximity. Proximity amplifies low levels of specialisation and lessens the interest in creating more elaborate task divisions.

To summarise our argument, we have retained the notion of *intrafunctional proximity* as a description of the reinforcement of the SME's low level of specialisation, and the notion of *coordination proximity* as a description of the preference of SME directors for mutual adjustment and direct supervision.

1. 3. From simple and informal internal and external information systems to proximity information systems

The main characteristic that defines the internal information systems of SMEs is simplicity and low structuring. The literature dealing with this specific field has often highlighted the preference of SME managers for the most informal media, and verbal information. According to Julien (1998), "small companies function by means of dialogue or direct contact. Conversely, large-scale organisations have to set up a complete formal (and written) mechanism to ensure that information is transmitted whilst simultaneously minimising rumours and encouraging control. Very large-scale organisations even publish an "in-house newspaper" to broadcast general information and prevent rumours from interfering with the company's efficiency". This preference for direct contact and verbal communication characterises the traditional operation of SMEs.

The external information systems of SMEs are also usually very simple because of a "relatively close market, either geographically or psychologically (…). This is how managers attentive to the slightest change in a market can rapidly become aware of changes in the local or regional traditional market; up to a certain point, this may offset their limitations in terms of expertise or the time available for thinking" (Julien and Marchesnay, 1988). In small companies, the owner-director functions by means of dialogue and direct contact with members of the staff as well as with his clients and suppliers, thus gaining direct knowledge of their needs and tastes, or explaining the different aspects of his products (Julien, 1998). The information systems are simple because they are based on close physical proximity between the SME's owner-director and the main leading players in the SME environment. Thus, through the study of the operation of a very small innovative business during its start-up phase, Planque (1988) shows that "the means of obtaining information are a group of interpersonal and informal relationships which are non-institutionalised and unstructured. Given the communication type used, the localisation of network "junctions" is mainly restricted to the area in which the prospective innovator might easily move around". This type of behaviour is directly linked to the characteristics of small organisations: the relational aspect is more important than the organisational aspect. Generally speaking, the direct link between spatial configurations and the firm's information capacities can be seen quite clearly here (Michun, 1994).

All in all, information systems in an SME context seem undersized. This characteristic is often interpreted as the consequence of the little interest certain company executives generally show in the strategic value of information (Chapellier, 1995). However, this undersizing may also be considered as the result of a concentrated spatial configuration favouring the setting up of direct, flexible and informal information systems. The proximity of the players facilitates direct and verbal communication; formalisation and writing are not essential. The often-observed link between proximity and a minimalist information management policy is thus understandable. We will adopt here the idea of *proximity information systems*.

1. 4. From intuitive, short-term and barely formalised, strategy to temporal proximity

"The cycle of strategic decision, in which SME time schemes are often short-term, is based on reaction rather than anticipation. Moreover, these companies use few management methods and techniques such as forecasting, financial analysis and project management. The decision-making process of SME managers is considered more intuitive, "informed guesswork", and less dependent on information and formal models of decision making" (Blili and Raymond, 1998). In SMEs, "the decision-making process usually works according to the intuition-decision-action pattern. The strategy is above all implicit and very flexible" (Julien and Marchesnay, 1988). Considering P.A. Julien's comments, the informal and intuitive characteristics that make up the specificity of SME strategy are explicitly founded on proximity: "Whereas large-scale companies have to draw up relatively precise "plans" for forthcoming actions that the company executives can refer to, the owner-managers of small companies are close enough to their key employees to explain every change of direction when necessary".

Similarly, the notions of reactivity, flexibility, interactivity and adaptability – qualities generally associated with SMEs - can be interpreted as being derived from a strong temporal proximity as well. These characteristics, specific to small companies, have "advantages of their own, such as rapidity for decision implementation, market proximity as well as a greater potential for adaptation and change of orientation in the short term" (Blili and Raymond, 1998). "The efficiency of SMEs is based on knowing how to take advantage of all local opportunities and resources in order to exploit market changes. For this very reason, production flexibility is inherently a matter of local flexibility. Organisational flexibility is "fundamentally local" as the different forms of flexibility are based more on tinkering than on standard and acknowledged know-how" (Courault, 1993).

Consequently, the preference for the short term, the intuitive aspect of strategic formulation and the qualities of flexibility and reactivity shown by SMEs are all characteristics based on the effects of proximity. To qualify this phenomenon, we will use the notion of *temporal proximity.*

1.5. From management specificity to proximity management

All the characteristics showing the specificity of SME management mentioned above can be considered as a particular form of proximity. The concept of SME defined by Julien (1990; 1998) can be understood as a *proximity mix* (Table 1).

Hierarchical, intrafunctional, temporal and spatial proximity (to name but four) make up a coherent framework producing the conditions required for action and reflection within a centralised and non-specialised organisation, which consists of simple internal and external information systems and which favours informal and intuitive strategies. It is in this sense that proximity management, as we see it, is not confined to simple metric measurement. It is the choice-making principle for owner-managers. All other things being equal, the SME manager will opt for what is both geographically and temporally closer to him. This preference for proximity, and the ensuing management, is a strategic and organisational construction enabling the SME manager to keep control of his firm and its development.

This reformulation enables us to move from a descriptive approach (a mere listing of characteristics) to an explanatory approach (highlighting a superior principle). The latter combines all the features of SMEs around a federating mechanism (proximity) and transforms this mechanism into the essential requirement for the standard operation of an SME. In other words, our perspective is that of a specific management style for SMEs that obeys a *proximity principle* (Torrès, 2000, 2004).

Table 1: SMEs as a proximity *mix*

From management SPECIFICITY… ***(According to Julien, 1990)***	***…to PROXIMITY management*** ***(According to Torrès, 2000)***
Small size	*Spatial proximity*
Centralized management	*Hierarchical proximity*
Low level of specialization	*Intrafunctional proximity* *Coordination proximity*
Simple and informal information systems	*Proximity information systems*
Intuitive and short-term strategy	*Temporal proximity*

Source : Torrès (2000)

Emphasising the *proximity principle* as an operative and explanatory approach to SME management is the foundation of a genuine research programme in all fields of management: what is the role of proximity in marketing, in HRM, in the strategic management of SMEs? What is the influence, role and significance of the effects of proximity on small-sized companies? Do the effects of proximity play the same role, and with the same intensity, in all business sectors? It is easy to imagine that this type of research programme could cast considerable, and innovative, light on SME management practices. If SME management specificity does exist, it must have a name. For our part, we call it "proximity".

We have just seen that the management model for SMEs can be seen as a mix of proximity types. Hence our central question: in strictly financial terms, can we consider that proximity is also a fundamental characteristic of SME finance? In other words, can proximity provide a context for general analysis of the various financial specificities of SMEs?

2. The financial characteristics of the proximity management model for SMEs

If we focus on the financial question at its source, that is, the question of the constitution of the original capital used to finance the company, academic research is almost unanimous in considering that this capital is highly subject to the effects of proximity.

According to Ang (1991), "The capital structure issue for small firms differs from their large firms' counterpart in several ways. First, small businesses rely on different sources of funds. For new business, the primary sources are: owner's own savings and personal borrowings, friends and relatives, local banks, and small business related sources (venture capital companies, SBIC, Minotity SBIC, SBA…)" (Ang, 1991: 582). Osteryoung, Newman and Davies (2001) do not say anything different: "Usually the owner has a very personal ownership stake in the formative stages of the business and understandably does not want to lose control of the vision and the strategies that have predicated its future growth. As a consequence, the equity of such businesses is usually held by a very close circle of family and friends" (Osteryoung and al., 2001 : 250). Saint-Pierre (1999 : 212) consolidates this opinion by evoking the concept of "friendly capital" (or "love money"): "Friendly capital comes from relatives or close friends of the entrepreneur, or from any other person with a proximity relationship with him. This capital is often used for the start-up of the company, and the demands are relatively flexible. Bankers count on this source of financing for rebalancing the financial structure when a company asks to increase the sums borrowed or for new capital. It should also be mentioned that the possibility of counting on friendly capital in case of financial difficulty becomes an important key for survival for many SMEs". Similarly, Belletante's concept of "*financial territory"* (1991) or Crevoisier's concept of "*proximity capital*"[3] (1997) support our theory of a proximity principle in small business finance.

These arguments are an excellent starting point for the development of our theory. In this second part, we will thus demonstrate how the different forms of proximity mentioned earlier can also be found in the financial practices of SMEs. The aim is to describe the financial specificities of SMEs as multiple forms of proximity and to conclude that there is such a thing as proximity finance as an analytic context for SME finance.

2. 1. Hierarchical proximity in small business finance

The personalisation of financial management is very strong in the case of SMEs. This personalisation is observable first by considerable centralisation of financial decisions. Unlike the fields of trade, production and even HR, finance is the field most commonly reserved for the director. It is rare for the director to delegate this type of decision, which often has a strategic nature. This centralisation is such that according to Saint-Pierre (1999: 96), "in entrepreneurial firms, it is easy to predict that the personal characteristics (of the owner-director), such as his schooling, experience, age and so on, will have an influence on his financing decisions".

This hierarchical proximity is illustrated by the high concentration of capital in SMEs. It could be considered that the smaller the company, the more the capital is

[3] As further proof of the link between proximity and financing in SMEs, Corpataux (2003) showed in his doctoral thesis to what extent the draining of the regional financing circuit in Switzerland mainly had an impact on SMEs. In his opinion, "the result is that from now on, SMEs can grow in two ways. Either they enter the stock market, with all the technical problems that that entails for small organisations, or they sell out to large, international groups. In the 1990s, for example, all the brand names from the clock-making sector were taken over by large groups" (Corpataux, 2003: 116).

concentrated into the hands of the director, who also has the function of owner. The famous dissociation between the functions of direction and ownership highlighted in the 1930s by Berle and Means has little validity in the specific case of SMEs. The functions of direction are more often than not performed by the owner himself. These reasons strengthen the concept of what we call hierarchical proximity, that is, the fact that financial decisions are almost exclusively the realm of a company's direction.

This concentration is not only a given fact; it is often the result of will, or more exactly, a refusal to float the company. Floating the company is not made easy for SMEs because of the difficulty of obtaining access to the financial markets. Not only the cost, but also the restructuring necessarily associated with a flotation on the stock market, dissuade most SMEs. According to the Pecking Order Theory put forward by Myers (1984), use of the stock markets is always the last solution envisaged, with directors of SMEs generally preferring self-financing. Even if the venture-capital solution is more accessible, it still remains rare. Although venture-capital practices have been developping over the last few years, they are still relatively low in terms of numbers. This figure is even lower if it is compared to the very large number of SMES in a given country or in the world. It is thus easy to see the marginal nature of this type of financing. Most SMEs are owned by a single person or by a family whose objectives often respond to a desire to maintain the power within their company. It is for this reason that finance in SMEs is characterised by considerable hierarchical proximity.

Finally, the incidence of the personal guarantees demanded by bankers from their SME-owning clients should also be noted: "Banks would often require personal assets, guarantees and insurance policies as collateral" (Ang, 1991: 578). According to Osteryoung *et al.*, (2001), the personal guarantees are the result of bankers wanting to minimise risks: "In other words, the bank cannot recognize any difference between the small business and its owner. To ensure its own security, a bank usually wants to make the owner personally responsible for the obligations inherent in the loan contract and does so by requiring the owner to personally guarantee the advance. Clearly, the bank is reducing its risk by requiring personal guarantees but it must be recognized that this increases the exposure of the small-business owner in the case of default" (Osteryoung *et al.*, 2001 : 6).

The existence and importance of personal guarantees is also one of the financial specificities of SMEs…to such an extent that Osteryoung and Newman (1993) take this criterion as an essential element of their financial definition of SMEs. "They define a small business as one exhibiting :

- no publicly traded equity
- an actual or potential need for the owners of the firm to personally guarantee any existing or planned borrowing

"The second element of the Osteryoung and Newman definition recognizes the nature of the personal exposure of the owner of the smaller firm to the creditors of the business. In many circumstances personal guarantees are required by banks when such a business applies for a loan. With the guarantee the bank will look to both the firm's assets and to the personal assets of the owner as security for its loan. The actual or potential presence of a personal guarantee significantly increases the risk of the small-business owner when compared to the risk accepted by the owner of equity in a publicly traded (i.e., large) firm." (Osteryoung *et al.*, 2001 : 4-5).

This hierarchical proximity gives SMEs other particularities, such as the fact for example that "the directors of SMEs do not have a sufficiently diversified portfolio of financial assets. It is not uncommon to observe that the shares in their own company make up almost all of their financial property. They thus cannot benefit from the advantages of risk diversification, all the more so because they invest in their company, their profession, their know-how and their job" (Belletante and Levratto, 1995 : 12). Lyagoubi (2002 : 10) develop the same idea : "the principal shareholder is characterized by the proximity of his personal inheritance and that of the company. Investing the major part of its personal richness in the company, it cannot diversify its risk in an optimal way, its fortune is, so directly related to that of the company".

For this reason, the distinction between the distribution of dividends and other direct and/or indirect forms of payment for the director remain very unclear. "Owners in a partnership and subchapter S corporation could integrate personal incomes to minimize personal taxes. They would be indifferent between compensation or profit distributed from the firm" (Ang, 1991: 576). Osteryoung *et al.* (2001) make the same observation, considering that the owners of SMEs withdraw funds from their company by means of several mechanisms, and not only by the distribution of dividends. The preference for these mechanisms depends on fiscal aspects. "It is important for the analysis to distinguish between the payment of a dividend which rewards the capital, and the payment of a salary that rewards work" (Osteryoung *et al*., 2001 : 264). The owner can also pay himself more in kind by buying, for example, a new and more spacious office, or a more modern factory.

On the contrary, "the owner-director indirectly contributes to the financing of his company in the form of reduced salary or unpaid overtime" (Saint-Pierre, 1999 : 91). Through the amount of work put in and the energy expended, the director is often the first base of the company's financing. In this respect, it is not uncommon to see directors of SMEs using their own, personal credit cards to pay for certain purchases for their companies. This is even a very practical source of financing, according to Osteryoung *et al*. (2001 : 259): "Other sources of debt for the smaller-business owner include such arrangements as those available with credit cards. These are usually relatively expensive sources of finance – however, many successful small firms have been financed initially with their owner's credit cards".

The centralisation of financial decisions, the high concentration of capital in the hands of the director and/or his family, the often categoric refusal to float the capital with third parties, the role and importance of personal guarantees, the confusion between the assets of the director and those of the company… all these elements are reasons that give small business finance considerable hierarchical proximity, making the classic separation between business and entrepreneur almost impossible in SMEs. "This financial and human amalgamation is a considerable factor in the increase both in costs and the probability of bankruptcy" (Belletante and Levratto, 1995 : 12).

2. 2. Functional proximity in small business finance

The specialisation of tasks is less pronounced than in large companies. This distinctive general characteristic can also be found in the financial field.

The first element to point to functional proximity is the more or less marked absence of a financial department in SMEs. It is very rare for the director of an SME to recruit a financial director. In his theory of the five levels that specify evolution in the structure of an SME in the course of its growth, Basire (1976) considers that the appointment of a financial director occurs only from stage 4 onwards, that is, when the SME has reached a payroll of approximately two hundred, and considerably later than the appointment of a commercial or production director, but just before that of a Human Resources director (in Julien, 1998).

A financial department may emerge earlier when the company has decided to gain access to the financial market. In this case, the complexity of the financial data that must be produced justifies hiring someone skilled in finance. The requirements for financial transparency and legal obligations mean that a skilled financier must be hired full-time. Access to the financial market requires such a high level of structuring that several authors consider that the very fact of floating an SME's capital for the general public boils down to endowing the company with the status of "future large company". The demands that govern the activities of listed companies mean that the financial status of the companies that have decided to float themselves on the stock exchange are more similar to those of large companies than to those of most SMEs, which prefer to remain closed and to retain their confidential information (Saint-Pierre and Baudoin, 1995 : 192). But these situations are extremely rare in the case of SMEs. Under normal circumstances, it is the owner-director who acts as the financial director. If he has not had training in finance, it can be deduced that financial skills are often rudimentary in SMEs. As Ang (1991 : 576) observes, "the management team is not completed. It may lack a full complement of managerial talents with knowledge and skills in finance…".

At this level, the crucial role of the public account can be seen. The accountant is often considered to be the ideal contact in this field. Public accounts are frequently the first "experts" to act as consultants in small companies. It is thus from the network of proximity experts that the focus of the structuring and formalisation of financial policy is decided. For this reason, raising the director's awareness of the financial subtleties of his company's development depends highly on the active role played by the financial partners engaged in the company's capital.

This weakness in specialisation of tasks can also be observed in the management of bank relations. In a study on the financial comportment of young companies in the Greater Lyon area, Mahérault (2005) focuses on the relations with banks of SMEs and, in particular, the number of banks. The results show that 90% of the SMEs questioned use only one, or at most two, banks. In other words, SMEs often do not take advantage of the complementarity of their different banking partners. This means that not only is the multiplication of bank relations relatively limited, but more, it only very rarely responds to the motives of specialisation. The theory can thus be put forward that the low general level of specialisation in SMEs also affects its ways of conducting relations with its banks by making their bank contact play the role of a general financial practitioner. For this reason, the range of financial services to which SMEs can generally have access remains limited (Belletante, 1991 ; Belletante and Levratto, 1995 : 9-10).

2. 3. Proximity information systems in small business finance

The weight of networks is one characteristic of the specificities of SME management. The links made between the director and the financial environment are vital. It has emerged from the responses received that the efficacy of financial strategy is largely determined by the director's capacity to identify, then integrate, the multiple networks in his environment. We will see later in this paper that the diversity to be found in these networks is a considerable advantage. In other words, financial strategy is not independent of the relational capacities of the director and his closest colleagues.

For example, it is in the field of bank relations that this characteristic is the most marked. As we have already said, the number of banks with which SMEs deal rarely goes beyond two. This low number has an advantage: the possibility of investing more in a dense and frequent relationship with one's banker. Effectively, "the results of certain surveys show that directors tend to do business with only a few financial institutions (sometimes only one). It is more profitable to develop a good relationship with a banker, who ends up understanding the personality of the owner-director and accepts his own, personal way of making decisions" (St-Pierre and Baudouin, 1995).

Binks and Ennew (1997) go even further, recommending *participative behavior* between SMEs and their bank: “Clearly, perfect information is an unobtainable goal, but a *close working relationship* between bank and business can significantly improve information availability”. Later, they add: “While collateral may be one mechanism for reducing the adverse effects of information asymmetries, the development of a *close working relationship* is an alternative. An effective banking relationship, by its nature, must involve two parties. For bank and businesses to invest time and effort in developing and maintaining such relationships requires that there are discernible benefits from so doing. (…) Further analysis suggests that more participative relationship types are associated with benefits to the firm in the form of better financing conditions and better quality of service and benefits to the bank.

This proximity relationship does not only work with the traditional banker, but also with venture capitalists. “Venture capital investors know the sector of activity of the new companies they are financing, but, more than that, they live in the area in which they work. They are by definition local entrepreneurs who support the business owners they decide to help, advise and train for their own profit. The fact that venture capital is “patient” money that should, under normal circumstances, remain part of the company’s capital for an average of 5 to 7 years, adds to this commitment to the local level. Venture capital investors tend in a relatively marked manner to operate in proximity to the place in which they are set up, that is, generally within a radius of 80 to 150 kilometres. They differ from bankers in that they are not only investors, but also that they are used above all to appreciating the value of people and not taking out mortgages on the borrowers’ assets” (Arzeni, 1991 : 11).

This proximity also explains the sometimes exaggerated attraction that SMEs have for financial confidentiality. In this context, confidentiality refers to the intimate nature of the information that is divulged only to one’s very closest colleagues. Proximity in this context refers more to the idea of “enclosed” than to “closeness”, once again bringing us back to the ambivalent nature of proximity (Torrès, 2004). It is this love of confidential information that is transmitted in the face-to-face relations that explains the high degree of asymmetry of information regarding new potential shareholders. For this reason, the latter tend to underestimate the future value of the company, which explains why resorting to an increase in capital can be particularly onerous. The cost of increasing the capital is proportional to the degree of asymmetry in the information. Specialists evoke the existence of “snared capital”. This is an essential concept for understanding the agency relations between minority shareholders and owner-directors of non floated companies. The illiquidity premium applied by risk capital companies bears witness to the importance of this aspect.

These proximity information systems also make it possible to describe the relations between directors and their shareholders: “Relationships with stockholders are less formal. The relationships between small business owners and outside stockholders are more implicit and less contractual. Owners/managers personally deal with their stockholders and thus, depending on the frequency of past and potential future transactions, personal reputation could be of value. Information collected on small business is often fragmented and private” (Ang, 1991: 576).

2. 4. Temporal proximity in small business finance

The fourth form of proximity that can be easily identified in SMEs is that of temporal proximity. Many studies have shown the preference of SME directors for the short term. This characteristic is illustrated in many ways in the case of finance.

In general terms, financial analysis of SMEs highlights two constant elements:

- weakness in the stable capital, that is, in the equity capital and financial resources of bank or non-bank origin in the mid- and long term
- short term over-borrowing which is seen in SMEs’ massive use of short term credit facilities, overdraft facilities or discounts, explaining why the behavioural standards adopted are dictated more by the search for flexibility in short term reactions than anything else (Ang, 1991; Norton, 1991; Belletante and Levratto, 1995).

Both these characteristics have been observed in several countries, including the United States, France, the United Kingdom, Israel and Japan (Saint-Pierre, 1999 : 96). This observation is in line with that of Hugues (1992 in Storey, 2000 : 215) : "The basic findings for the asset and liability structures of small companies are broadly similar to those of previous investigations in the 1960s and 1970s. The high reliance on short term finance provided by banks, and the relatively low proportions of assets financed by shareholders' interests are clearly long run persistent features of small business finance. The same is true of the relative importance of trade debt and trade credit and the relative unimportance of fixed assets in their balance sheet structure".

This temporal proximity that favours the short term over the long term also has an impact on the financial criteria used. For example, directors of SMEs can be more sensitive to a short payback period than to a high internal rate of return. Similarly, liquidity is often preferred in SMEs, sometimes even to the detriment of profitability which refers to a more distant temporal horizon. Osteryoung *et al*. (2001) even go as far as considering that this dependency on liquidity restricts investment capacities in SMEs: "smaller firms are more dependent on liquidity. As a result, there are a number of new ideas about the capital-investment decision in smaller firms that concentrate on the liquidity issue". (Osteryoung *et al*., 2001 : 186). The preference for liquidity is evidence of the predominance of the short term over the long term, and thus of temporal proximity.

Temporal proximity is also identifiable in the slightest financial planning of SMEs in comparison with large companies. And, even when SMEs do plan ahead, generally speaking the time scales are more restricted than those of large companies. All this means that directors of SMEs often admit that they do not have a financial policy, whilst regretting that they have neither the time nor the skills to take care of things better. They often recognise that they have a "case-by-case" type of management, where opportunism is the key and planning the exception.

Conclusion: towards a *proximity mix* finance

At the end of our analysis, it appears that the different forms of proximity governing the general management of SMEs can also be observed in the particular field of finance. Our central theme is that finance in SMEs is subject to the effects of proximity that result in specific behaviour. The following table summarises our arguments.

From management SPECIFICITY… **(According to Julien, 1990)**	***…to PROXIMITY management*** **(According to Torrès, 2000)**	**... and its financial implications**
Small size	*Spatial proximity*	- Proximity capital - Love money - Predilection for geographically close key players (bankers, venture-capitalists..)
Centralized management	*Hierarchical proximity*	- Centralised financial decisions - Concentration of capital in the hands of the owner or his family - Refusal to float the capital - Personal guarantees - Pecking Order Theory
Low level of specialization	*Functional proximity* *Coordination proximity*	- Restricted range of financial services on offer - Absence of financial director or department - Preference for a limited number of financial partners
Simple and informal information systems	*Proximity information systems*	- Preference for direct and personalised relations - Predilection for confidentiality - Relational investment recommended
Intuitive and short-term strategy	*Temporal proximity*	- Short term over-borrowing - Preference for liquidity - Insufficient equity capital - Absence or relative weakness in financial planning

Table 2: SMEs finance as a proximity *mix*

There is one last point that deserves to be mentioned. This is Myers' Pecking Order Theory. Many empirical validations of Myers' pecking order theory (1984) for financial choices as applied to the field of SMEs stipulate that the growth of SMEs is essentially financed by internal funding, i.e., funding from profits retained by the business to fund its growth, then by debt, rather than by issuing share capital (opening the capital) (Norton, 1991; St-Pierre and Baudouin, 1995; Mahérault, 1999). “For small business, the pecking order theory needs some adjustment to reflect the difficulties associated with financing its activities. Initially there will be a preference for start-up equity and retained earnings. Once the business proves its creditworthiness, debt financing becomes an option. It is in the area of the third preference, that of equity, that the small business differs from its larger cousin. While equity is publicly available, at least in theory, in the case of the larger business, it is rarely available to the same extent for the small business. However, the order of preference remains the same for both large and small business.” (Osteryoung *et al*., 2001 : 263)

However, it can be observed that the Pecking Order Theory is based implicitly on proximity. Proximity is high in the case of self-financing, average in the case of bank relations and low in the situation of access to the financial market. Under these conditions, our proximity criterion remains valid but changes status. It is no longer a simple descriptive context, it has become an explicative factor! This research axis almost certainly merits more in-depth study.

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