

7 March 2011

For information

Legislative Council Panel on Financial Affairs

SME Financing Guarantee Scheme

Purpose

This paper briefs Members on the SME Financing Guarantee Scheme that was launched by The Hong Kong Mortgage Corporation Limited (HKMC) on 1 January 2011.

Background

1 Small and medium-sized enterprises (SMEs) are an important pillar of economy and employment in Hong Kong. About half of the total workforce in Hong Kong is employed by the SMEs. In 2008, the collapse of Lehman Brothers caused credit crunch and market dislocation around the world. To mitigate the impact of the global financial crisis, the Government of the Hong Kong Special Administrative Region swiftly rolled out the HK\$100 billion Special Loan Guarantee Scheme to help SMEs resolve the difficulty in obtaining bank financing and the potential surge in unemployment problems due to closing down of SMEs. With the recovery of the local economy as well as the improved financing and cash flows for SMEs, the Special Loan Guarantee Scheme ceased to receive new applications from 1 January 2011.

2 Back in May 2010, many SMEs and think tanks proposed that Hong Kong should develop a sustainable, market-oriented platform to guarantee SME loans upon the phasing out of the Special Loan Guarantee Scheme. This proposal gained extensive support from society. The SMEs and banks believed that the HKMC's financial strength and track record in operating financing guarantee and insurance businesses would make the HKMC a good candidate to offer a sustainable, market-

based SME financing guarantee scheme. This would help banks to manage their lending risks more effectively and in turn provide SMEs with more stable financing.

3 The HKMC therefore carried out extensive consultation with stakeholders (including SME associations, banks, accounting firm, etc.) and studied the proposition, and then obtained approval from the Board of Directors in mid-November 2010 to launch the SME Financing Guarantee Scheme based on prudent commercial principles from 1 January 2011. The Scheme will be effective in lowering banks’ credit risk on lending to the SMEs and help maintain the stability of the banking sector, which is in line with the core objectives of the HKMC.

The SME Financing Guarantee Scheme

Objectives and Merits of the Scheme

4 The SME Financing Guarantee Scheme aims to provide a flexible, market-oriented scheme with a wider scope of guarantee protection to help the SMEs in Hong Kong obtain more stable financing from banks for meeting their funding needs on working capital or acquisition of equipment and assets to support their business operations. For the banks, the Scheme helps banks to better manage their lending risks and is instrumental in enhancing the stability of the banking sector.

Major Features

(a) Target Segment and Eligibility	<p>Enterprise must have been in operation for at least one year in Hong Kong as at the date of guarantee application</p> <p>Enterprise shall have and continue to have business operation in Hong Kong and shall have been registered under the Business Registration Ordinance (Chapter 310) (excluding listed companies, lending institutions and</p>
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	<p>affiliates of lending institutions)</p> <p>With sound loan repayment record</p>
(b) Facility Approval Decision	Approval of facility is to be done by the lenders
(c) Guarantee Coverage	50%, 60% or 70%
(d) Maximum Guarantee Period	5 years
(e) Maximum Facility Amount	<p>HK\$12 million</p> <p>(There is no ceiling on overall guarantee commitment by the HKMC under the Scheme)</p>
(f) Re-use of repaid facility amount	No restriction on the number of loan applications, headroom produced within the Maximum Facility Amount after repayment to term loans can be re-used for new credit facilities
(g) Forms of Facilities	Cover term loans and revolving credit lines without any limitation on the proportion between the two types of facilities
(h) Use of Proceeds	<p>The proceeds from the facility must be used for providing general working capital , or acquisition of equipment or assets (excluding residential properties) for the enterprise' business operations</p> <p>The proceeds from the facility must not be used for repaying, restructuring or repackaging existing debts</p>
(i) Maximum Loan Interest Rate	8% per annum in general
(j) Personal Guarantee by Individual Shareholder(s)	Personal guarantee by individual shareholder(s), directly or indirectly, holding more than 50% of the equity interest of the enterprise is required
(k) Guarantee Fee	For core products, the annual guarantee fee rate ranges from around 0.5% to 2.5% of the facility amount

	Guarantee fee can be settled by single upfront payment or annual payment (it is an option to finance the single upfront guarantee fee payment by the initial drawdown of the facility)
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Complementing Existing Guarantee Schemes and Facilities For the SMEs

5 During the design stage of the SME Financing Guarantee Scheme, the HKMC has made reference to various support schemes offered by different departments of the Government with a view to forging synergy. In relation to the SME Loan Guarantee Scheme operated by the Trade and Industry Department (TID), the HKMC's SME Financing Guarantee Scheme complements by providing more sustainable financing and also flexibility to the SMEs. For example, the SME Financing Guarantee Scheme has not set any Scheme ceiling on the overall guarantee commitment by the HKMC. Non-listed enterprises may also apply for protection under the Scheme which offers a more extensive coverage of banks' corporate lending products. The Scheme allows both term loans and revolving credit facilities without any limit on the proportion between the two forms of facilities, and there can be recycling of the limits for repaid facilities for use by new credit facilities. Details are in Annex.

Operation of the SME Financing Guarantee Scheme

6 The SME Financing Guarantee Scheme complements existing support schemes or arrangements provided by the Hong Kong Government to help SMEs in business development and enhance their competitiveness in the market. The HKMC has also set up a support team to work closely with lenders on promotional and product development activities, such as amending the loan underwriting policies, operational manuals, credit documents and operational systems, staff training, product promotion, etc. Some of the lenders have launched related products by phases in the

market. As at 28 February this year, the HKMC has received 16 applications from six lenders involving facility amount of around HK\$47.5 million. We have anticipated that there will not be very high business volume at the early stage of the Scheme. However, the global market conditions are very volatile and there is a high degree of uncertainty, which may change the business and financing environments for the SMEs. In those circumstances, the SME Financing Guarantee Scheme will play an important role to encourage banks to continue to provide stable and sustainable financing to the SMEs by unloading SME exposure to the HKMC as necessary. The HKMC will maintain its dialogue with the stakeholders and make appropriate refinements to the Scheme in response to changes in market conditions.

The Hong Kong Mortgage Corporation Limited
28 February 2011

**Comparison between the SME Financing Guarantee Scheme and
the two loan guarantee schemes offered by the TID**

Product Features	SME Loan Guarantee Scheme offered by the TID	Special Loan Guarantee Scheme offered by the TID (no new applications after 31 December 2010)	SME Financing Guarantee Scheme offered by the HKMC
Scheme Guarantee Commitment	HK\$20 billion	HK\$100 billion	No ceiling
Use of Proceeds	<ul style="list-style-type: none"> ▪ For acquiring business installations and equipment relating to the enterprise's business operations ▪ For meeting working capital needs of general business uses 	<ul style="list-style-type: none"> ▪ For meeting the needs of general business uses 	<ul style="list-style-type: none"> ▪ For meeting working capital needs of general business uses ▪ For acquiring equipment or assets relating to the enterprise's business operations (including industrial or commercial properties, but excluding residential properties)
Guarantee Ceiling under the Scheme	50% of the approved loan	70% or 80% of the approved loan (the former applicable to applications submitted to the TID before 15 June 2009, whereas the latter applicable to applications submitted on or after the date)	Options available: 50%, 60% and 70%
Maximum Guarantee Amount / Maximum Facility Amount	Maximum Guarantee Amount of <u>HK\$6 million</u>	Maximum Loan Amount of <u>HK\$12 million</u>	Maximum Loan Amount of <u>HK\$12 million</u>

Product Features	SME Loan Guarantee Scheme offered by the TID	Special Loan Guarantee Scheme offered by the TID (no new applications after 31 December 2010)	SME Financing Guarantee Scheme offered by the HKMC
Reuse of Guarantee Amount / Facility Amount after repayment	Maximum Guarantee Amount can be reused for <u>one time</u>	Not allowed	Unlimited reuse of Guarantee Amount
Form of Facilities	Term loans (<u>excluding</u> revolving credit facilities)	Term loans and revolving credit facilities, but the revolving credit facilities cannot exceed 50% of the Maximum Loan Amount (i.e. HK\$6 million)	Term loans and revolving credit facilities, without the 50% limit on revolving credit facilities
Eligibility	<ul style="list-style-type: none"> ▪ For SMEs only ▪ With substantive business operation in Hong Kong ▪ No need to have one year business operation history 	<ul style="list-style-type: none"> ▪ All enterprises registered in Hong Kong (excluding listed companies and lending institutions) ▪ With substantive business operation in Hong Kong ▪ Incorporated before 15 December 2007 	<ul style="list-style-type: none"> ▪ With one year business operation history in Hong Kong ▪ No restriction on the date of incorporation
Application Processing Time	Respond in 3 days		Respond in 3 days
Claim Processing Time	1 month		10 days