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Panel on Commerce and Industry

Meeting on 20 March 2018

**Updated background brief on support measures for
small and medium enterprises**

Purpose

This paper provides updated background information on a series of support measures currently administered by the Administration for small and medium enterprises ("SMEs"), including three SME funding schemes (i.e. SME Loan Guarantee Scheme ("SGS"), SME Export Marketing Fund ("EMF") and SME Development Fund ("SDF")), and the SME Financing Guarantee Scheme ("SFGS") and its Special Concessionary Measures. This paper also provides updated background information on the Dedicated Fund on Branding, Upgrading and Domestic Sales ("BUD Fund"), and provides a summary of the views and concerns expressed by members on the subjects in previous discussions.

Background

2. There are about 330 000 SMEs¹ in Hong Kong which constitute over 98% of Hong Kong's business establishments and employ about 46% of the workforce in the private sector.² Their vitality and business performance are of crucial importance to the development of Hong Kong's economy. Over the years, the Administration has been providing assistance to SMEs through various funding schemes having regard to prevailing economic situation to support their continuous development.

¹ According to the Trade and Industry Department ("TID"), Small and Medium Enterprises ("SMEs") are manufacturing enterprises with fewer than 100 employees and non-manufacturing enterprises with fewer than 50 employees in Hong Kong.

² The figures as provided by TID are updated as at September 2017.

Small and medium enterprise funding schemes

3. To help SMEs secure finance, expand export markets, upgrade human resources and enhance their competitiveness, a number of SME funding schemes, namely SGS,³ EMF,⁴ SDF⁵ and the SME Training Fund,⁶ were established in December 2001/January 2002. In late 2008, the Administration further introduced the Special Loan Guarantee Scheme ("SpGS") to help enterprises secure loans from the participating lending institutions ("PLIs") for meeting general business needs to tide over the liquidity problem during the global financial crisis with the Government acting as the guarantor. SpGS subsequently ended in late 2010.⁷

4. In order to help SMEs grasp economic opportunities and boost their competitiveness, the Financial Secretary ("FS") announced in his 2018-19

³ SME Loan Guarantee Scheme aims to help SMEs secure loans from participating lending institutions for acquiring business installations and equipment, and meeting working capital needs, with the Government acting as the guarantor. The amount of guarantee for an SME is 50% of the approved loan. The guarantee can be used to secure loans for business installations and equipment and working capital, subject to a maximum total guarantee amount of \$6 million. The guarantee period is up to five years. As at 28 February 2018, out of the 33 995 cumulative applications received, 30 968 applications were approved, the cumulative amount of loan approved was over \$52 billion.

⁴ SME Export Marketing Fund provides direct subsidy to SMEs for participation in export promotion activities, including local or overseas trade exhibitions, overseas business missions, and placing advertisements in printed trade publications or trade websites targeting export markets, so as to encourage enterprises in expanding their export business. For each successful application, the maximum amount of grant will be 50% of the total approved expenditures incurred by the applicant or \$50,000, whichever is the lower. As at 23 February 2018, out of the 254 820 cumulative applications received, 215 479 applications were approved, the total amount of grants approved was over \$3.2 billion.

⁵ SME Development Fund provides financial support to non-profit-distributing organizations to implement projects which aim at enhancing the competitiveness of Hong Kong's SMEs in general or in specific sectors. The maximum amount of funding support for each approved project is \$5 million, or 90% of the approved project expenditure, whichever is the lower. The successful applicant is required to contribute the remaining 10% of the total project expenditure, which may be in cash, in kind or in the form of sponsorship. Each project should be completed within three years. As at 31 January 2018, out of the 1 142 cumulative applications received, 284 applications were approved, the cumulative amount of grants approved was over \$345 million.

⁶ Launched in January 2002, the SME Training Fund ("STF") supported SME employers and employees to take up training courses relevant to their business operation. In view of the significant duplication between STF and other training and education initiatives which employers and employees of SMEs could obtain Government support, the Government ceased accepting new STF applications from July 2005.

⁷ As at 28 February 2018, a total of 39 275 applications were approved under the Special Loan Guarantee Scheme, the cumulative amount of loan approved was over \$94 billion.

Budget⁸ the following enhancements on EMF and SDF:

- (a) injecting \$1 billion into EMF and SDF; and
- (b) increasing the cumulative funding ceiling for enterprises under EMF from \$200,000 to \$400,000, and removing the existing condition on the use of the last \$50,000 of grants.

Previous discussions

5. The Administration briefed the Panel on Commerce and Industry ("the Panel") at the meeting on 16 June 2015 on its proposal to inject \$1.5 billion into EMF and SDF; increase the maximum amount of funding support for each project under SDF from \$2 million to \$5 million, and extend the maximum duration of each project from two years to three years; and expand the scope of EMF to cover more types of export promotion activities. With the Panel's support for the aforesaid proposal, the Finance Committee ("FC") approved the funding on 17 July 2015. The Panel was also briefed by the Administration on the latest progress of these SME funding schemes on 18 April and 17 October 2017. Members' views and concerns are summarized in the ensuing paragraphs.

6. At the Panel meeting on 16 June 2015, members expressed concern over the decline in the number of EMF applications from some 27 000 in 2010 to some 17 000 in 2014. The Administration advised that in view of the sluggish performance of the traditional export markets in Europe and the United States since the global economic downturn induced by the worldwide financial turmoil in end 2008, SMEs were more prudent in carrying out export promotion activities, or had reduced promotion activities. The Administration also observed that, with the rapid advancement and prevalence of Internet technology to carry out export promotion activities, there had been a declining trend for SMEs to make use of traditional channels for export promotion.

7. Members were also concerned about the low application success rate of SDF (only 50% of the applications were approved between April 2014 and February 2015), and enquired whether the objectives of SDF would overlap with that of the BUD Fund (details of the BUD Fund are in paragraphs 21 to 37). The Administration advised that it had been encouraging non-profit-distributing organizations, in particular trade and industrial organizations to apply for SDF. Unsuccessful applicants were informed of the reasons of rejection and meetings would be arranged to help them revise and re-submit

⁸ The Financial Secretary also announced to provide a total of \$250 million additional funding to the Hong Kong Trade Development Council in the five financial years from 2018-19 for assisting local enterprises (SMEs in particular) in seizing opportunities arising from the Belt and Road Initiative and the Guangdong-Hong Kong-Macao Bay Area development, promoting the development of e-commerce, and enhancing Hong Kong's role as a premier international convention, exhibition and sourcing centre.

their applications if they so wished. Many rejected applications were eventually approved. The Administration further explained that the Enterprise Support Programme ("ESP") of the BUD Fund aimed at assisting Hong Kong enterprises in exploring and developing the Mainland market, and the Organization Support Programme ("OSP") of the BUD Fund provided funding support to non-profit-distributing organizations to undertake projects which could assist Hong Kong enterprises in developing brands, upgrading operations and developing domestic sales in the Mainland. On the other hand, SDF provided funding support for non-profit-distributing organizations to implement projects that could enhance the competitiveness of SMEs, including exploring overseas markets, without any geographical restriction.

8. At the policy briefing cum meeting on 17 October 2017, the Administration noted members' suggestions of raising the amount of grant under EMF for export promotion activities and business missions relating to the Belt and Road Initiative, and allowing more flexibility in the funding scheme by relaxing the restriction that the last \$50,000 of grants had to be used for an enterprise's participation in export promotion activities which were not any of those funded by the first \$150,000 of the grants received by the enterprise.

Small and Medium Enterprise Financing Guarantee Scheme

9. The Hong Kong Mortgage Corporation Limited ("HKMC") launched the market-based self-financing SFGS on 1 January 2011, with a view to helping Hong Kong enterprises, particularly SMEs, to obtain financing to meet their needs. Under SFGS, HKMC acts as guarantor for up to 70% of the approved loans that enterprises obtain from PLIs. A guarantee fee is payable by the PLIs/enterprises. The interest rate of each loan is a commercial decision made by PLIs.

10. To tide enterprises, particularly SMEs, over a possible credit crunch as a result of credit tightening under the uncertain external economic environment, the Government provided a total loan guarantee commitment of \$100 billion for HKMC to launch time-limited special concessionary measures⁹ under SFGS on 31 May 2012. With the special concessionary measures, 80% guarantee is provided at a substantially reduced guarantee fee.

11. Starting on 1 June 2016, the annual guarantee fee rate for the measures was reduced by 10% and the minimum guarantee fee of 0.5% for the measures was also removed.

⁹ The maximum loan amount to be guaranteed under the special concessionary measures for each enterprise and its group of related enterprises at any one time is \$12 million (including revolving loans), and the maximum guarantee period for each approved loan is five years.

12. The original application period for the special concessionary measures was 9 months until end of February 2013. In view of the challenging external economic environment, the Administration extended the application period for the special concessionary measures under SFGS five times to the end of February 2018. To further help SMEs to boost their competitiveness, FS announced in his 2018-19 Budget that the application period for the special concessionary measures under SFGS be extended to 28 February 2019.

13. According to the Administration, the high overall success rate of applications (the rate stood at 99.3% as at 28 February 2017) indicated that the measure was effective in assisting SMEs in obtaining loans from banks. Besides, the special concessionary measures helped lower the borrowing cost that the average total lending cost of loans approved under the special concessionary measures was 5.32% p.a. (comprising the average loan interest rate of 4.82% and the average guarantee fee rate of 0.5%). This further compared favourably with the average total lending cost of loans approved with 50%/60%/70% guarantees under SFGS, which was 6.81% p.a. (comprising the average overall interest rate of 5.26% and the average guarantee fee rate of 1.55%).

14. According to the Hong Kong Monetary Authority, as at 31 December 2017, HKMC approved 12 844 applications under the special concessionary measures involving a total loan amount of around \$51.2 billion. Of the applications approved, over 70% of the applicants were from the non-manufacturing sector and around 22% from the manufacturing sector.

Previous discussions

15. The Panel discussed the support measures for SMEs, including SFGS, at the meetings on 16 April 2013, 21 October 2014 and 18 April 2017. Members also discussed the effectiveness of the special concessionary measures under SFGS at the special meeting of FC for examination of the Estimates of Expenditure 2017-18 on 6 April 2017.

16. At the Panel meeting on 16 April 2013, some members asked whether the Administration had taken any action to discuss the interest rate issue with PLIs. The Administration advised that SFGS including the special concessionary measures was a market-based loan guarantee scheme. The interest rate of each commercial loan was a commercial decision made by PLIs after taking into account a basket of factors including the borrower's operational, financial and repayment capability; the type and nature of credit facility; as well as the type and quality of any security pledged. The Administration had no plan to discuss the interest rate issue with PLIs for the time being.

17. At the Panel meeting on 21 October 2014, some members remarked that SGS and SFGS which offered guarantees for a loan size of up to \$12 million could not benefit SME retailers as most of these SMEs might require only a small loan size of under \$1 million, preferably interest-free and available quickly to address their pressing cash-flow problem. The Administration advised that SGS and SFGS provided guarantees for a loan of any size which was under \$12 million. As at the time of the meeting, over 1 400 approved cases of the special concessionary measures under SFGS involved a facility amount of \$1 million or below.

18. At the Panel meeting on 18 April 2017, some members relayed that many enterprises found the cost of applying for loans under the special concessionary measures high because of the need to pay the guarantee fee. Members then urged the Administration to consider re-launching SpGS which ended in 2010 and was welcomed by many enterprises owing to free-of-charge applications. The Administration pointed out the average loan amount of the special concessionary measures under SFGS (over \$3.98 million) was higher than that under SpGS (about \$2.35 million). As for the lending cost of loans approved under the special concessionary measures under SFGS, it was also relatively low given that 97% of the loan applications approved did not require collateral.

19. At the FC meeting on 6 April 2017 and the Panel meeting on 18 April 2017, some members pointed out that the respective numbers of applications received and approved, as well as the facility amount for applications approved under SFGS were on the decline in the past three years. Members enquired whether the numbers had been increased after the Administration's introduction of the reduction of the annual guarantee fee rate and removal of the minimum guarantee fee in June 2016. The Administration advised that HKMC had streamlined some of the application procedures in coordination with PLIs and launched a publicity campaign for SFGS since the second quarter of 2016. The number of applications for the special concessionary measures had increased by 15% in the second half of 2016 compared to the first half of that year; and by 45% in the first quarter of 2017 compared to the same period in 2016.

20. Noting that only 175 out of a total of 775 net default claims under SFGS were approved and compensated (as at 28 February 2017) and HKMC had completed only 94 claim cases in 2016, some members urged the Administration to accelerate the processing of unsettled claim cases. The Administration responded that HKMC would normally respond to PLIs within 10 working days upon receipt of its default claim. While HKMC had been actively processing the outstanding default claims, the primary reason why HKMC could not be able to complete the vetting of these claims was that the PLIs concerned had yet to provide HKMC with all the required information and documents for the due diligence review.

Dedicated Fund on Branding, Upgrading and Domestic Sales

21. The National 12th Five-Year Plan emphasizes expanding domestic demand as well as the upgrading and restructuring of industries. To help Hong Kong enterprises capture the opportunities arising from the National 12th Five-Year Plan, the then Chief Executive announced in his 2011-12 Policy Address the proposal to set up a \$1 billion BUD Fund to assist enterprises in exploring and developing the Mainland market through developing brands, upgrading and restructuring their operations and promoting domestic sales in the Mainland.

22. Following the funding approval by FC on 11 May 2012, the BUD Fund was launched on 25 June 2012. Subject to the funding balance, the BUD Fund was initially planned to be open for applications for five years, and the tenure may be reviewed and extended, if necessary. The uncommitted balance of the BUD Fund as at end of February 2017 stood at around \$459 million (representing 45.9% of the total commitment approved). FS announced in the 2017-18 Budget the extension of the application period of the BUD Fund for another five years to June 2022 to continue to assist Hong Kong enterprises in furthering their business development in the Mainland. The BUD Fund comprises two programmes, namely ESP and OSP.

23. In 2018-19 Budget, FS further announced his proposal to inject another \$1.5 billion into the BUD Fund. He also proposed to enhance ESP under the BUD Fund, details of which are in the following paragraphs.

Enterprise Support Programme

24. ESP provides funding support to individual Hong Kong enterprises in undertaking projects to develop brands, upgrade and restructure their business operations and promote sales in the Mainland market, so as to enhance their competitiveness and facilitate their business development in the Mainland market. All non-listed enterprises registered in Hong Kong under the Business Registration Ordinance (Cap. 310) with substantive business operations in Hong Kong are eligible to apply for funding under ESP. In his 2018-19 Budget, FS announced his proposal to extend the geographical scope of ESP from the Mainland to include the countries of the Association of Southeast Asian Nations ("ASEAN").

25. Funding of ESP is provided on a matching basis, i.e. the Government will cover a maximum of 50% of the total approved project cost and the enterprise has to contribute no less than 50% of the total approved project cost in cash. During the tenure of the BUD Fund, each enterprise may obtain funding for a maximum of three approved projects. Each project should be completed within 24 months. In his 2018-19 Budget, FS announced an increase of the cumulative funding ceiling per enterprise under ESP from \$500,000 to \$1,000,000 for them to undertake projects in the Mainland and ASEAN markets.

26. Under the ESP Easy – Simplified Application Track ("ESP Easy") launched in August 2015, applicant enterprises are only required to fill in a simplified application form. Funding will be provided on a matching basis after completion of projects, and the funding ceiling for each project is \$200,000. All ESP Easy projects must be completed within 12 months. Funding approved for projects under ESP Easy will be counted towards the cumulative funding ceiling per enterprise under ESP; and each enterprise can obtain funding for a maximum of three projects under ESP (including ESP Easy).

27. A "Simplified Option" under the normal track of applications was also launched in October 2016. It allows applicants to commence projects as early as after the date of submission of applications and waives the requirement of setting up a separate project account should the applicants opt not to receive initial payment of funding.

28. Up to end of February 2017, a total of 2 087 applications had been processed. For the 2 087 applications, excluding the 493 applications subsequently withdrawn by the enterprises, there were 1 594 applications, amongst which 806 were approved. The total amount of funding approved was about \$287 million.

Organization Support Programme

29. OSP provides funding support to non-profit-distributing organizations to undertake projects which can assist Hong Kong enterprises in general or in specific sectors in developing their brands, upgrading and restructuring their business operations, and promoting domestic sales in the Mainland so as to enhance their overall competitiveness in the Mainland market.

30. The maximum amount of funding support for each approved project is \$5 million, or 90% of the approved project expenditure, whichever is the lower. The applicant has to contribute the remaining 10% of the project expenditure, which may be in cash, in kind or in the form of sponsorship. The maximum duration of a project is three years.

31. As at 31 January 2018, the cumulative number of applications received was 200, among which 70 applications were approved, 89 applications were rejected and 35 applications were withdrawn. The total amount of grants approved was over \$223 million.

Previous discussion

32. The Panel discussed the latest progress of the BUD Fund at the meeting on 18 April 2017. The major views and concerns of members are summarized below.

33. Members noted the unspent funding in the BUD Fund was substantial and the success rate of ESP applications remained low despite members' suggestions of introducing promotion and publicity to enhance enterprises' understanding of the application criteria and procedure of ESP made at the Panel meeting on 17 March 2015. Members enquired about the cause of such a low success rate even after the Administration's efforts to step up relevant promotion and publicity, and suggested increasing the batches of applications accepted in a year and raising the funding level for better utilization of the funding. The Administration advised that the number of applications received had increased with the overall success rate of ESP applications after the launch of a host of improvement measures.

34. Some members noticed that some companies that assisted SMEs in applying for ESP had charged a considerable sum for their services provided. They urged the Administration to provide more assistance to the applicant enterprises in the application process, so that such enterprises would not have to seek the assistance of intermediaries, and could dedicate the approved funding to effectively implement the projects.

35. The Administration responded that while under ESP, enterprises might apply for funding to engage a qualified service provider to help them develop a holistic business plan, particular attention had been paid to expenses related to engagement of consultants when vetting the applications to ensure that they would not make up an unreasonably high proportion of the approved funding for a project.

36. Some members enquired whether the funded enterprises would share their experience in implementing the funded projects and the real benefits brought about by the projects to the development of their businesses and tips for successful applications. The Administration advised that a guidebook (available at the ESP website and distributed free of charge) had been published on the experiences of enterprises from various industries in implementing the funded projects under ESP and the effectiveness of such projects. Besides, the funded enterprises had also been invited to share with other interested enterprises their experiences in implementing the funded projects and the real benefits brought about by the projects to the development of their businesses.

37. Some members asked how the BUD Fund could assist enterprises which were adversely affected by the growth of e-commerce. The Administration replied that enterprises could apply for funding to undertake specified activities which could effectively assist them in enhancing their competitiveness in the Mainland and developing the Mainland market. These activities included the establishment or enhancement of websites or online shops.

Council question

38. At the Council meeting of 26 May 2016, Mr Jeffery LAM asked a written question on, among other things, whether the Administration had adequate preparation and formulated corresponding measures for assisting SMEs in tiding over economic downturn, and whether the Government would re-launch SpGS.

39. The Administration responded that to help SMEs secure loans in the commercial lending market and lower their loan cost, FS announced in the 2016-17 Budget that the Administration would extend the application period of the special concessionary measures under SFGS to 28 February 2017. The Administration would also continue to implement various SME funding schemes to assist SMEs in obtaining financing, opening up markets and enhancing competitiveness, including the BUD Fund. Since amid the uncertain external economic environment, the Administration had implemented the special concessionary measures under SFGS, and that SMEs might obtain loans under the regular SGS, the Administration considered that there was no need to re-launch SpGS.

Latest position

40. The Administration will brief the Panel on 20 March 2018 on the implementation progress of various funding schemes including the BUD Fund and the special concessionary measures under SFGS, and seek members' support of the funding proposals for the proposed enhancement measures on the funding schemes. The Administration will also receive deputations' views on the subject matters at the meeting.

Relevant papers

41. A list of relevant papers is in the **Appendix**.

Appendix

List of relevant papers

Date of meeting	Meeting	Paper
16/4/2013	Panel on Commerce Industry	<p>Administration's paper on "Support measures for small and medium enterprises" (LC Paper No. CB(1)832/12-13(07))</p> <p>Background brief on support measures for small and medium enterprises prepared by the Legislative Council Secretariat (LC Paper No. CB(1)832/12-13(08))</p> <p>Minutes of meeting (LC Paper No. CB(1)1280/12-13)</p>
15/4/2014	Panel on Commerce and Industry	<p>Administration's paper on "Progress report on the implementation of the Dedicated Fund on Branding, Upgrading and Domestic Sales" (LC Paper No. CB(1)1236/13-14(03))</p> <p>Updated background brief on the Dedicated Fund on Branding, Upgrading and Domestic Sales prepared by the Legislative Council Secretariat (LC Paper No. CB(1)1236/13-14(04))</p> <p>Minutes of meeting (LC Paper No. CB(1)1593/13-14)</p>
21/10/2014	Panel on Commerce and Industry	<p>Administration's paper on "Government assistance for small and medium enterprises affected by 'Occupy Central'" (LC Paper No. CB(1)53/14-15(08))</p> <p>Minutes of meeting (LC Paper No. CB(1)212/14-15)</p>

Date of meeting	Meeting	Paper
17/3/2015	Panel on Commerce and Industry	<p>Administration's paper on "Report on the progress of implementation of the Dedicated Fund on Branding, Upgrading and Domestic Sales" (LC Paper No. CB(1)632/14-15(03))</p> <p>Background brief on the Dedicated Fund on Branding, Upgrading and Domestic Sales prepared by the Legislative Council Secretariat (LC Paper No. CB(1)632/14-15(04))</p> <p>Minutes of meeting (LC Paper No. CB(1)819/14-15)</p>
16/6/2015	Panel on Commerce and Industry	<p>Administration's paper on "Funding Injection and Enhancement Measures for SME Development Fund and SME Export Marketing Fund" (LC Paper No. CB(1)971/14-15(05))</p> <p>Background brief on the increase in commitment and enhancement measures for SME Development Fund and SME Export Marketing Fund prepared by the Legislative Council Secretariat (LC Paper No. CB(1)971/14-15(06))</p> <p>Minutes of meeting (LC Paper No. CB(1)1223/14-15)</p>
17/7/2015	Finance Committee	<p>Administration's paper on "SME Export Marketing and Development Funds" (FCR(2015-16)26)</p> <p>Minutes of meeting (LC Paper No. FC67/15-16)</p>
21/4/2016 (issue date)	Panel on Commerce and Industry	<p>Administration's paper on "SME Financing Guarantee Scheme – Special Concessionary Measures" (LC Paper No. CB(1)831/15-16(01))</p>

Date of meeting	Meeting	Paper
25/5/2016	Council	Question No. 10 on "Assisting SMEs in tiding over economic downturn" raised by Hon Jeffery LAM (Hansard) (page 10228 – 10233)
18/4/2017	Panel on Commerce and Industry	Administration's paper on "Extension and Progress Report of the Dedicated Fund on Branding, Upgrading and Domestic Sales and the Special Concessionary Measures under the SME Financing Guarantee Scheme" (LC Paper No. CB(1)779/16-17(05)) Background brief on support measures for small and medium enterprises prepared by the Legislative Council Secretariat (LC Paper No. CB(1)779/16-17(06)) Minutes of meeting (LC Paper No. CB(1)1145/16-17)
12/6/2017 (issue date)	Finance Committee	Administration's paper on "Extension of the Application Period of the Dedicated Fund on Branding, Upgrading and Domestic Sales" (FCRI(2017-18)7)