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Panel on Commerce and Industry

Meeting on 17 March 2020

Updated background brief on the SME Financing Guarantee Scheme

Purpose

This paper provides updated background information on the SME Financing Guarantee Scheme ("SFGS"), and a summary of the views and concerns expressed by members of the Panel on Commerce and Industry ("the Panel") during the last discussion on the subject.

Background

2. The Hong Kong Mortgage Corporation Limited¹ ("HKMC") launched the market-based self-financing SFGS on 1 January 2011 with a view to helping Hong Kong enterprises, particularly small and medium enterprises ("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 the participating lending institutions ("PLIs"). A guarantee fee is payable by the PLIs/enterprises. The interest rate of each loan is a commercial decision made by PLIs.

Special concessionary measures: 80% guarantee product

3. In May 2012, the Government provided a total loan guarantee commitment of HK\$100 billion for HKMC to launch time-limited special concessionary measures under SFGS to tide enterprises over a possible credit crunch as a result of credit tightening under the uncertain external economic

¹ To cope with the business development of the Hong Kong Mortgage Corporation Limited ("HKMC"), effective from 1 May 2018, the SME Financing Guarantee Scheme business has been transferred to and carried out by the HKMC Insurance Limited, a wholly owned subsidiary of HKMC.

environment. With the special concessionary measures, 80% guarantee is provided at a substantially reduced guarantee fee. The application period of the special concessionary measures was initially nine months (from 31 May 2012 to 28 February 2013). Given the uncertainties in the external economic environment prevailed and to help enterprises grasp economic opportunities, the Government had extended the application period several times to 30 June 2022.

4. With effect from 19 November 2018, the Government launched the following three enhancement measures to further relieve the financing burden of local SMEs and help them to obtain financing:²

- (a) halving the annual guarantee fee rate;
- (b) increasing the maximum facility amount from HK\$12 million to HK\$15 million; and
- (c) lengthening the maximum guarantee period from five years to seven years.

5. With effect from 4 September 2019, both existing and new SME borrowers may apply to their PLIs under SFGS for principal moratorium of up to six months which is renewable, subject to a maximum of 12 months in total. During such period, only interest payments have to be made. The guarantee period can be extended correspondingly, but should not exceed the maximum guarantee period of seven years, with guarantee fee payable to cover the extension of the guarantee period. The new relief measure will last for one year.

6. As at 21 February 2020, 17 553 applications were approved and the total loan amount involved was over HK\$73 billion. The cumulative expenditure for settling default claims, expected default claims under processing and out-of-pocket expenses incurred were about HK\$2 billion (up to 31 August 2018), representing around 18% of the HK\$11 billion expected maximum expenditure to be incurred by the Government under the special concessionary measures.

90% guarantee product

7. In 2019, the Government introduced a new loan guarantee product under SFGS with a total loan guarantee commitment of HK\$33 billion to provide additional support to smaller-sized enterprises and businesses with relatively less operating experience, as well as professionals seeking to set up their own practices. Under this new product, 90% guarantee is provided for approved

² The validity period of the enhancement measures was initially about seven months (until 30 June 2019), which was then extended several times to 30 June 2022.

loans taken out by eligible enterprises from PLIs. Following the approval of the Finance Committee ("FC") on 6 December 2019, the HKMC Insurance Limited ("HKMCI") started receiving applications on 16 December 2019. The application period will last until 30 June 2022.

8. The terms applicable to the 90% guarantee product are similar to those for the 80% guarantee product except that there is no requirement on business operation history. Besides, the maximum loan guarantee period for each approved loan under the 90% guarantee product is five years from the first drawdown of the facility. Having regard to the needs of the target beneficiaries and the need to control risk exposure of the Government, the maximum amount of loans each enterprise can obtain guarantee under the 90% guarantee product is HK\$6 million at any point in time.

9. As at 21 February 2020, 252 applications were approved and the total loan amount involved was over HK\$428 million. The Government's estimated maximum expenditure under the 90% guarantee product is around HK\$5.4 billion.

Special 100% guarantee product

10. In order to support enterprises and safeguard jobs under the tough economic environment, the Financial Secretary ("FS") has proposed in the 2020-2021 Budget to introduce a concessionary low-interest loan under SFGS, under which 100% guarantee (up to HK\$20 billion) will be provided by the Government.

11. FS has further proposed that the application period will last for six months. The maximum amount of loan for eligible enterprises is based on their salary and rental expenditures for six months, subject to a ceiling of HK\$2 million. The repayment period is up to three years and, on an opt-in basis, a principal moratorium is available for the first six months during which only interest payments has to be made.

Last discussion on the subject

12. The Administration sought the Panel's support on the proposed introduction of the 90% guarantee product at the meeting on 29 October 2019. The major views and concerns expressed by members are summarized in the ensuing paragraphs.

13. Members noted that the maximum amount of loans each successful applicant could obtain loan guarantee under the proposed 90% guarantee product (i.e. up to HK\$6 million at any point in time) was far below from that of

the 80% guarantee product (i.e. up to HK\$15 million), and enquired about the reasons for such differences.

14. The Administration advised that the proposed 90% guarantee product aimed to help enterprises tide over potential financing difficulties amidst the economic downturn, and provide additional support to enterprises with less operating experience, limited credit history, and those enterprises lacking the expertise or resources to produce financial statements. The maximum amount of loans each enterprise could obtain loan guarantee under the proposed 90% guarantee product would be capped at HK\$6 million at any point in time. The banking industry and relevant organizations and major stakeholders generally supported the proposed 90% guarantee product and called for early implementation.

15. Some members also pointed out that although the maximum loan interest rate for the proposed 90% guarantee product (8% per annum for enterprises with operating history of more than three years) was lower than that of the 80% guarantee product (10% per annum in general), there were concerns from the trade that the loan interest rate for the proposed 90% guarantee product might still be too high for them to afford. They asked whether the Administration would consider providing 100% guarantee for approved commercial loans so that PLIs would no longer be subject to any default risks and could greatly reduce the loan interest rates for SMEs to obtain financing.

16. The Administration advised that following the implementation of the enhancement measures for the 80% guarantee product as stated in paragraph 4 above, the number of approved applications and the additional loan amount in the first nine months of 2019 had increased year-on-year by 70% and 107% respectively, reflecting the effectiveness of the new measures in assisting enterprises in loan financing. Yet, some smaller-sized enterprises and enterprises with less operating experience might not be eligible for the 80% guarantee product. In order to bridge the gap, the proposed 90% guarantee product would lift the requirements on the one year's minimum operation of applicants and the submission of full audited financial statements.

17. The Administration also advised that SMEs participating at a recent SME Symposium were generally of the view that the average loan interest rates as disclosed by two different PLIs were lower than expected. SMEs could also benefit from a competitive market by comparing offers from different PLIs and negotiate a deal.

Council question

18. At the Council meeting of 26 February 2020, Hon CHUNG Kwok-pan asked a written question on whether the Administration would discuss with the banking industry the simplification of the procedure for vetting and approval of SME loan applications and the relaxation of the application criteria, so as to resolve the financing difficulties encountered by SMEs.

19. The Administration advised that to strengthen funding support to SMEs, the Hong Kong Monetary Authority ("HKMA") had established a banking sector SME lending coordination mechanism. Three meetings were held in October 2019, January and February 2020 respectively under the coordination mechanism. The meetings were attended by representatives from the Hong Kong Association of Banks, major banks active in SME lending, and HKMCI. Banks attending the meeting agreed to adopt a series of measures to strengthen support to SMEs. Key measures adopted by banks included:

- (a) making good use of the countercyclical capital buffer released by HKMA to support SMEs;
- (b) allowing SMEs to extend or reschedule their repayment period so as to relieve their cash flow pressure, having regard to HKMA's clarification of credit risk management requirements;
- (c) introducing relief measures targeting specific sectors (such as the import and export and transportation sectors) to facilitate fund flow management by SMEs; and
- (d) following the guidelines set out in the "Hong Kong Approach to Corporate Difficulties" to handle SMEs encountering financial difficulties with sympathy and enhanced communication, and to avoid withdrawing credit lines hastily or taking other credit actions that would adversely affect the customers' business operations.

20. HKMCI and banks had also simplified the application procedures for SFGS, such as by accepting other forms of financial proof in lieu of financial statements where appropriate. In view of possible changes to loan guarantee terms as necessitated by banks' extension of loan tenors and trade financing repayment schedules, HKMCI had streamlined procedures to expedite processing of bank applications for revision of loan terms. HKMA, in collaboration with HKMCI and banks, would also hold briefing sessions for SMEs to explain banks' lending procedures and SFGS. HKMA, together with the banking sector, would continue to maintain close dialogue with the commercial sector with a view to providing appropriate support to SMEs and helping them cope with the economic challenges.

Latest position

21. The Administration will brief the Panel on 17 March 2020 on the proposed introduction of a new product under SFGS, under which the Government will provide 100% guarantee for concessionary low-interest loans and a guarantee commitment up to HK\$20 billion. Subject to members' views, the Administration will submit the relevant financial proposal to FC for approval.

Relevant papers

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

Council Business Division 1
Legislative Council Secretariat
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Appendix

List of relevant papers

Date of meeting	Meeting	Paper
29/10/2019	Panel on Commerce and Industry	Administration's paper on "Enhanced Support to Small and Medium Enterprises" (LC Paper No. CB(1)34/19-20(06)) Updated background brief on support measures for Hong Kong enterprises prepared by the Legislative Council Secretariat (LC Paper No. CB(1)34/19-20(07)) Minutes of meeting (LC Paper No. CB(1)246/19-20)
29/11/2019 & 6/12/2019	Finance Committee	Administration's paper on a package of measures to relieve people's financial burden and support enterprises (FCR(2019-20)39)
26/2/2020	Council	Question No. 7 on "Financing of small and medium enterprises" raised by Hon CHUNG Kwok-pan (Government press release)