

## Wu Xiaoling: Promoting the extension of micro credit

Speech by Ms Wu Xiaoling, Deputy Governor of the People's Bank of China at the Videoconference on promoting the extension of micro credit, Beijing, 6 July 2004.

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Ladies and Gentlemen,

Deputy Secretary-General of the State Council Mr. You Quan has just conveyed the instruction of Vice Premier Mr. HUANG Ju to the conference, representatives from 5 different provinces and cities have introduced their experiences in micro credit extension, and relevant speakers from the Ministry of Finance, the Ministry of Labor and Social Security and the China Banking Regulatory Commission have also specified their plans for promoting the extension of micro credit. As leaders of the State Council are much attentive to the making of micro guaranteed credit policy on unemployed laid-off workers, so banking system should seriously study the spirit of Vice Premier Huang Ju's instructions and learn from the advanced experiences of the 5 provinces and cities to facilitate the work of micro guaranteed credit for unemployed laid-off workers to make new breakthroughs continually. I will focus my speech on the following issues in terms of banking system's responsibilities.

Since the micro guaranteed credit business started in 2002, the People's Bank of China, the Ministry of Finance and the Ministry of Labor and Social Security have consecutively issued a series of policy documents, which stipulate the target borrowers, loan size, maturity, guarantee and interest subsidy. With joint efforts of all relevant parties, micro credit policy has developed extensively in the whole country and become one of the most important reemployment policies to support laid-off workers to find jobs and start up business on their own. By end-May of 2004, the outstanding amount of micro credit to laid-off workers extended by all financial institutions reached RMB1.22 billion yuan, among which, RMB590 million yuan was extended in the period from January to May in 2004. Employees in the banking system have made great contribution to the development of micro-credit business.

We have two pieces of precious experiences drawn from nearly two-year implementation of micro credit policy. First, banking credit support alone cannot satisfy the need of laid-off workers to find jobs and start up business on their own, therefore, reemployment policy should be assisted by necessary job training and employment services by way of combining job training with micro credits to raise the successful reemployment ratio effectively; second, because laid-off workers have limited ability to start up their own business and most of them still need to be absorbed by enterprises, in addition to micro credit extension, we should strengthen credit support to small and medium sized enterprises, in particular small labor-intensive enterprises which can absorb many laid-off workers. According to our investigation and feedbacks from relevant parties, the following problems exist in implementation of micro credit policy: first, lack of policy publicity and many local governments did not understand or misunderstood the policy; second, in some places complicated credit approval procedures and high guarantee requirements hindered borrowing; third, lack of proper projects and high credit management cost discouraged lending activity; and fourth, in some places, lack of coordination among different departments resulted in low efficiency.

On March 18<sup>th</sup>, given the emerged problems in reemployment efforts and experiences from different regions, the People's Bank of China, the Ministry of Finance and the Ministry of Labor and Social Security jointly issued the *Circular on Promoting Micro Credit to Unemployed Laid-off Workers (Bank Document 2004 No.51)* to adjust and improve relevant policies. Promoting the implementation of micro credit policy relies on the following five aspects:

### **1. Improve risk-sharing and compensatory mechanism for micro credit; effectively streamline loan guarantee and approval procedures.**

The core issue of enlarging micro credit extension is to ensure risk compensation. At the beginning, various guarantee funds were set up by local fiscal departments and managed by guarantee institutions to share micro credit risks. But in practices, many guarantee institutions require laid-off workers to provide counter guarantee. The purpose of guarantee fund is to disseminate micro credit risks and possible losses incurred by start-up businesses, with proper counter guarantee, a laid-off worker could borrow directly from a bank without resort to the guarantee fund. The reason they go to guarantee fund is just because of their high risk profile. In some places, counter guarantee

requirements restrained substantially micro credit extension. *No.51 Bank Document* clarifies risk-sharing principles. If some regions have already chosen guarantee institutions, counter guarantee cannot exceed 30 percent of the total credit extension; furthermore, with strengthened credit management system, each region should abolish counter guarantee requirement gradually. For regions that have not chosen guarantee institutions, their fiscal departments can deposit guarantee funds into banks which can extend micro credits to the laid-off workers independently. In the event the extend loans went sour, 20 percent of the resulted losses should be borne by the issuing bank and the other 80 percent be absorbed by the guarantee funds, among which, provincial fiscal departments shall assume 10 percent of the losses while the other 70 percent is to be assumed by low level fiscal departments. By this arrangement, banks, provincial and local fiscal authorities could share risks effectively. Besides, credit extension efficiency is improved with banks directly involved in credit approval.

## **2. Introduce the experience of combining job training with micro credits, support laid-off workers to start-up business of their own.**

To improve laid-off workers' ability to start-up their own businesses, most cities have launched job training program. Based on such practice, the People's Bank of China and the Ministry of Labor and Social Security jointly promoted the application of "job training plus micro credits" model in 100 cities, which is to provide qualified trainees on a selective basis with credit guarantee, lower counter guarantee threshold and encourage micro credit extensions by financial institutions. Combing job training with micro credits should become a standard way for commercial banks to extend micro credit in the future, including not only fiscal subsidized loans, but also many other commercial micro credits to promote labor market development. All branches (Operations Offices) and sub-branches of the People's Bank of China in the capital cities of each province should directly supervise this task in two or three cities joining the pilot program and strengthen relevant researches. Commercial banks should also explore further in this regard and spread successful experiences nationwide.

## **3. Strengthen credit support for small enterprises to absorb more job-seekers**

Small enterprises are the main sources for employment. Due to both historical and personal reasons, many laid-off workers even subject to job training still cannot start up their own businesses and thus seek to be reemployed through job application. Therefore, government has issued various policies to support small enterprises to absorb laid-off workers. In accordance with *No.51 Bank Document*, small labor-intensive enterprises, which absorb laid-off workers by over 30 percent of the total number of current employees and sign employment contract for above one year, will enjoy three preferences in receiving micro-credit: First, 50 percent of the interest rate set by the People's Bank of China will be subsidized by the fiscal authorities with the central and local fiscal departments each contributing half of the subsidy fund; Second, 10 percent of bank's micro loan losses will be covered evenly by the central and local fiscal departments; Third, local fiscal departments pay issuing commercial banks 0.5 percent of commission fees. Total micro credits extended to each small enterprise could reach as high as RMB1 million yuan with a maximum of 2-year maturity, based on a credit line of 20,000 yuan for each laid-off workers. Although it appears that such preferential policies are not very attractive, since the interest rate of credit to small enterprises could float 70 percent above the benchmark rate, commercial banks should be able to completely cover their risks by increasing the risk premium. Furthermore, interest and loan losses subsidies should help relieve the commercial banks' political worries about credit extension to small enterprises, especially to the private-owned small enterprises. I hope commercial banks could understand this policy and strengthen their credit support to small labor-intensive enterprises so that they could absorb many laid-off workers.

## **4. Effectively use social security platforms at communities to establish credit communities.**

Extension of micro credits involves large workloads, substantial management costs and high risks. Rural credit cooperatives have solved such problems by establishing credit households, credit villages and credit towns. In recent years, established urban communities have become the basis of China's political hierarchy and social development in the sense that reemployment services for laid-off workers, social services for retired workers and benefits distribution for low-income households all are conducted on the community platform. Because communities understand most deeply local

enterprises and households, especially laid-off workers whose livings rely on community services, it is useful to establish a good financial environment and reduce micro credits management costs and risks by establishing credit communities and publicizing financial knowledge. Credit community will benefit not only micro credit extension but also other types of loan extension. I wish every commercial bank could participate in the establishment of credit community; in particular, branches of the People's Bank of China at all levels should assist labor and social security departments to establish credit communities to promote implementation of micro credit extensions to laid-off workers.

**5. Help small and medium sized financial institutions to define appropriate market niche in order for them to provide communities with quality financial services.**

Although we have many national financial institutions, they are not suitable to extend micro credits due to long management chains. Social financial services call for community banking services providers that focus on serving local households. Micro credit businesses are mostly based in cities and conducted by branches and outlets of financial institutions which are located in urban communities. Branches of the People's Bank of China at all levels should work closely with the China Banking Regulatory Commission to cultivate development of community banks and help small and medium sized financial institutions to define appropriate market niche, effectively tap market potentials and strengthen support to reemployment efforts.

Ladies and Gentlemen, policy implementation holds the key to success of guaranteed micro credit business. Concerning the interests of laid-off workers and even social stability, extension of micro credit is indeed a solemn political task which can only be accomplished with hard work and quality services. The people's Bank of China should coordinate with fiscal departments at all levels to establish guarantee funds and other fiscal subsidies in time and improve the efficiency of guarantee institutions. Besides, the People's Bank of China should work closely with the labor and social security departments to make feasible plans to promote job training and micro credit extension for laid-off workers, foster the establishment of credit community, and conduct periodical evaluation of various support schemes. All commercial banks, especially local financial institutions should adjust their own credit management in accordance with new regulations and support development of the small and medium sized enterprises to contribute to the coordinated social and economic development.