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Promoting Inclusive Finance for Real Economy in China

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Improving policies and systems for inclusive finance

In recent years, the Central Committee of the Communist Party of China and the State Council have attached high importance to the development of inclusive finance. At the Fifth National Financial Work Conference in 2017, General Secretary Xi Jinping put great emphasis on building an inclusive financial system and extending financial services to small and micro enterprises (SMEs), agriculture, rural areas, rural people, and remote areas, to promote targeted financial poverty alleviation. During the State Council's executive meeting chaired by Premier Li Keqiang, policies and measures had been discussed to make financing more accessible and affordable for SMEs and to encourage financial institutions to grant more loans to them. Under the guidance of the People's Bank of China (PBC) and regulatory authorities, Yi Gang, governor of the PBC said at the Lujiazui Forum 2018 that the PBC would work with related departments to jointly improve associated financial services for SMEs. Guo Shuqing, Chairman of the China Banking and Insurance Regulatory Commission (CBIRC) headed the survey to further solve the financing difficulties of private enterprises and SMEs. Later, the PBC, the CBIRC, the Ministry of Finance, the China Securities Regulatory Commission, and the National Development and Reform Commission jointly issued "Opinions on Further Deepening Financial Services for Small and Micro Enterprises" and encouraged financial institutions to offer more financial supports for SMEs, agriculture, rural areas, rural people, and private sector to reduce their funding costs. In September 2018, China officially set up the national financing guarantee fund. Currently, the policy environment and the relevant systems have become more favorable for developing inclusive finance.

Emphasizing practical effects in inclusive finance development

Banking financial institutions are advocating and actively promoting inclusive finance development. Wider coverage of basic financial services and increased financial accessibility in weak

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fields have enhanced the efficiency and quality of inclusive financial services, and the positive results are mainly shown in the following six aspects.

First, different types of banking financial institutions are better positioning themselves in the marketplace and driving strategic transformation. Large commercial banks have played the leading role in setting up an inclusive finance department and an operating mechanism covering comprehensive services, statistics accounting, risk management, resource allocation, and assessment and appraisal, to improve inclusive financial services. For example, in 2018, Industrial and Commercial Bank of China set the strategic goal of annually increasing the loans in inclusive finance by over 30% and doubling the figure in the subsequent three years; China Construction Bank (CCB) expressed that it would strive to implement inclusive finance strategy on all fronts. Currently, large state-owned banks have set up inclusive finance departments at the head office and at all 185 tier-one branches. Share-holding banks have accelerated exploring the establishment of inclusive finance departments considering their own business features and have set up over 5,000 grassroots-level communities and other sub-branches serving SMEs. China Minsheng Bank, Industrial Bank Co., Ltd., China Zheshang Bank, and other three banks have set up inclusive finance departments while China Merchants Bank and China CITIC Bank have established inclusive financial service centers. Local banking financial institutions focus on helping the local economy and serving SMEs by increasing their coverage of inclusive financial services and extending their operation and service to counties, towns, and villages, where people have limited access to financial services.

Second, more credit loan are supplied, and inclusive financial services are more accessible. By the end of June 2018, loan balance to SMEs nationwide had grown by 13.06% over the previous year to reach RMB32.35 trillion, an increase of RMB1.55 trillion from the beginning of the year. The number of borrowers increased by 2.8182 million from the same period last year to reach 16.9905 million. The loan balance to SMEs with line of credit less than RMB10 million surged by 16.03% to RMB8.46 trillion over the same period of the previous year, and the growth rate was 1.92 percentage points higher than that of other types of loans. During the same period, the borrowers with loan balance also rose to 14.8199 million, an increase of 3.1788 million over the same period of the previous year. Agriculture-related loan balance stood at RMB32.16 trillion, up by 7.3% over the same period of the previous year, among which loan balance related to farming, forestry, animal husbandry, and fishery and supporting agriculture stood at RMB14.46 trillion, an increase of 6.82% over the same period of the previous year; loan balance in rural areas reached RMB26.07 trillion, an increase of 6.9% over the same period last year; and loan balance of rural people reached RMB8.81 trillion, an increase of 14.6% over the same period of the previous year.

Third, there has been concentration on weak fields and steady enhancement on financial support for targeted poverty alleviation. At the end of June 2018, poverty-reducing micro-credit balance reached RMB259.712 billion and the number of registered poor households reached 6.3873 million, an increase of RMB10.016 billion and 312,900, respectively, from the beginning of the year. Loans per household stood at RMB40,700, accounting for 27.59% of the national total.

Fourth, the coverage of basic financial services has become wider with greater convenience. At the end of 2017, there were a total of 228,700 banking outlets nationwide, among which 7,890 were community outlets, 2,550 were outlets serving SMEs, 960,600 were ATMs, and 31.1886 million were POS terminals. Outlets of financial institutions or mobile services have covered 161,100 administrative villages of 832 state-supported poverty-stricken counties, with a 95.65% coverage. National basic financial services have covered 531,300 administrative villages, that is, 96.44% coverage.

Fifth, innovative financial products and service models have remarkably improved the quality and efficiency of financial services. In addition to financial services targeting traditional enterprises, banking financial institutions are using financial technology to innovate service channels and improve the quality and efficiency of services. For example, CCB extends credit based on the existing whitelist and explores the entire process of online financing service called "Fast Loan to Small and Micro Businesses." In 2017, the number of new borrowers exceeded 140,000, granted loans reached RMB146.6 billion, and the rate of non-performing loans was 0.16%. Zhejiang MYBank Co., Ltd. operates mainly online and offers its "310" loan services. That means it takes three minutes to make an online application, one second for lending assessment, and zero manual intervention. WeBank launched "Weilidai," its "micro-loan" to grant loans using Big Data credit ratings. Customers applying for credit can receive their application result within 2.4 seconds and funds draw-down within 40 seconds, experiencing more convenience and efficiency.

Sixth, there has been a reduction in the financing cost in inclusive finance to serve the real economy. Banking financial institutions are practicing inclusive finance by properly setting the price of loans for SMEs to lower their financing cost. Recently, large banks are taking the lead in reducing the interest rates of loans granted to SMEs. For example, Postal Savings Bank of China helps SMEs reduce their financing costs by 53 basis points from the beginning of 2018 (6.09% for the first half of the year, and 5.56% for September), shortens the financing chain, follows relevant policies to renew loans, and seamlessly renews loans granted to SMEs. It continues to reduce charges and commissions, overhaul unnecessary intermediate stages, and put a ban on charging SMEs for loan commitment, funds management, financial consultancy, and advice to ease the financing burden of SMEs from the source. In 2017, large- and medium-sized commercial banks canceled 335 charging items targeting inclusive finance customers and reduced or canceled fees of 387 items, reducing fees totaled RMB36.7 billion for the whole year.

Promoting the development of inclusive finance

Despite the achievements made in the development of China's inclusive finance, and against the background of rising downward pressure on economic growth and growing international trade conflicts, the development of inclusive finance is confronted with increasing pressure and challenges mainly in the following four areas. First, the monetary transmission mechanism should be improved and the banking financial institutions' risk preference needs to be adjusted. Even when inter-bank market liquidity was ample and the interest rate of the deposits and loans remained unadjusted in the first half of 2018, the interest rate for financing in some regions and industries rose slightly. So private enterprises and SMEs still felt the financial pressure. Under risk management in the banking industry, banks should increase their support to private enterprises and SMEs while keeping risks under control or being able to take more risks. Second, financial services provided to SMEs, agriculture, rural areas, and rural people, and poor population are still costly and risky in the conventional mode. Commercial sustainability faces great challenges, and inclusive financial services lack endogenous growth. Third, it needs to overcome challenges and refine inclusive financial system more systemically and institutionally. Meanwhile, the problem that some policies fail to be adequately implemented needs to be resolved. Fourth, the lack of standards, services differentiation, and problems in information security existing in this new type of financial sector have brought financial chaos to inclusive finance innovation. Bearing the above-mentioned issues in mind, the banking sector may solve the "last mile" problem of inclusive finance through the following six aspects.

Creating a favorable business environment to make financing accessible to SMEs and private enterprises

Banking institutions alone cannot solve the problem of inaccessibility to financing, so joint efforts are required. First, synergy between the departments of finance, industry and commerce, taxation, and regulation, is needed to introduce policies and to create an environment of information sharing and cooperation for a win-win outcome for inclusive finance. Second, given that the corporate governance and financial statements of SMEs are not standard, the average life cycle of such enterprises lasts around three years, and effective guarantee or collateral is missing, it is urgent to standardize the financial management, improve the credit information system, make such enterprises more risk-resistant, and bridge the gap between SMEs and private enterprises with commercial banks to solve information asymmetry. The third issue is the development of the supply chain finance that meets the financing demands of SMEs and private enterprises, and granting credit to and managing upstream and downstream enterprises in the supply chain using lot-sizing principle to improve the efficiency and quality of credit services. The fourth issue is the promotion of venture investments including angel investment and venture capital investment, guiding venture capital and private equity to flow to small businesses in their early periods and accelerating multi-layered capital market and financial innovation.

Broadening the financing channels and making financing more affordable to SMEs and private enterprises

At present, it is expensive for SMEs to raise funds. Financing fees remain high largely due to market factors. Both the banks and the government should play their roles through market means and policy measures. Currently, the interest rates on loans granted to SMEs by large- and medium-sized banks generally floats upward no more than 30% of the benchmark interest rate, and more fees reductions are being made. In contrast, the interest rates on loans granted by institutions other than commercial banks is relatively high. For example, the monthly interest rates of private financing in some regions of Jiangsu Province and Zhejiang Province generally stays above 1% while that of interim bridge financing may even exceed 3%. Under such circumstances, banking institutions should comply with relevant requirements of "two growths and two controls," coordinate the amount and price of such loans while properly setting the interest rate on microcredit and ensure the commercial sustainability of inclusive financial services. In addition, the policy of renewing loans without repayment of principal needs to be better implemented to address the problem of capital turnover confronting SMEs while renewing loans, and to lower SMEs' cost of obtaining interim working capital from market institutions.

Innovating financial products and business model to improve the quality and efficiency of financial services

The financing demands of SMEs are usually urgent and frequent. It has a short loan period and is strict in loan limit. Accordingly, banking financial institutions need to provide different types of comprehensive financial services according to the enterprises' development stage. Besides, based on the assets condition and the financing demands of SMEs, medium- and long-term financing products should be launched, and resource allocation should be further optimized to add a variety of guarantees and collaterals, shorten the financing workflow, and improve financial services.

Using the incentive and assessment mechanism to increase the endogenous driving forces of inclusive financial services

Inclusive financial services are widely dispersed. It is strict in loan limit and is low in cost-to-profit ratio. To resolve these problems, efforts should be made in the following two aspects. The first is complying with the regulation requirements, specifying due diligence and liability exemption methods, improving the incentive and constraint mechanism, and more rationally selecting the assessment and appraisal indicators and performance assessment scheme, to increase the endogenous driving forces of inclusive financial services. The second is devising a separate inclusive finance credit plan, and allocating more financial resources to key areas and weak links in the development of the real economy, and thereby better meet the demands of SMEs, agriculture, rural areas, and rural people for diversified financial services.

Employing financial technology to support the development of SMEs and prevent risks while enhancing efficiency

In the technology-driven era, banking financial institutions must exploit technology innovation, Big Data, artificial intelligence, cloud computing, and other advanced technologies to offer services more precisely through data mining and analysis of customers. Meanwhile, Big Data should be applied to more fields including customer marketing, anti-fraud, risk pre-warning, supply chain finance, micro-credit, and data security, for controlling risk and improving the efficiency of credit granting and approval, and therefore improving customer experience.

Establishing and improving an effective risk compensation and financing guarantee mechanism

Establishing and improving the

risk compensation mechanism and guaranteeing a system targeting SMEs is an important part of making financing more affordable and accessible for them. Relevant efforts can be made in the following three aspects. The first is setting up an effective risk compensation mechanism, and exploring models including fiscal interest subsidies and cooperation between taxation departments and financial institutions. The second is co-building a financing guarantee system, forming a micro-credit risk sharing model featuring "government + banks + insurance," and strengthening the risk guarantee for SMEs, agriculture, rural areas, and rural people. The third is building and improving the relevant legal system, regulating the market, and keeping the industry in order.

Providing inclusive financial services is a challenging and long-term task. In recent years, banking financial institutions are actively engaged in the innovation and development of inclusive finance and constantly draw lessons from practices and gradually find a new path to develop inclusive finance. However, inclusive finance cannot be made accessible and affordable overnight, and there is a long way to go before covering the "last mile," which requires brainstorming and synergy between the policy makers, regulators, practitioners, and scholars.

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