China MSME Finance Report 2016

(Compact Edition)

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China MSME Finance Report 2016

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ISBN 978-7-5049-7601-7/F.7161

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Acknowledgments

The Chinese version of this report has been prepared by a core team led by Shi Jianping and Yang Rubing, comprising Bi Cheng, Chen Yan, Ding Jingfeng, Ding Qi, Feng Jianhua, Gao Mengying, Gao Yao, Li Shanshan, Liu Qing, Liu Yitong, Shi Xiuhong, Shi Yucheng, Tong Yi, Wang Jian, Wang Tingting, Wang Wanting, Wang Wei, Wu Kai, Xie Junyao, Xu Xiaohua, Xu Jin, You Meiqi, Zeng Lianyun, Zhang Hongbin, Zhang Jie, Zhang Qianhe, Zhao Jiawei, Zhao Jianchuan, Zhao Yajuan, Zhou Xin. Zeng Lianyun was responsible for the translation of this English version.

We acknowledge financial support from the National Natural Science Foundation of China (NSFC) under grant number 71173247.

Deeply appreciate the scholars and experts who patiently accept our research and consulting on MSME finance. Their study provides very professional advice and practice experience. This report condenses their wisdom.

Preface

In 2015, economic growth of China was still faced with the situation where old forces were weakening, while new ones short, leaving economic downturn still stressful and business conditions tough. With respectively five consecutive times of interest and reserve rate cuts, in an effort to provide liquidity and bring down financing cost for enterprises within the year, funds that did flow to the real economy, or say, especially MSEs, were just a tiny proportion. ‘MSEs’ again appeared as a topic in executive meetings of the State Council.

At the same time, marketization reform carried on in depth and breath. Interest rate liberalization harvested crucial progress, with interest rate control fully ended since then, deposit insurance system was officially built, financial infrastructure, including credit inquiry system, was improved, and the construction of a multi-level capital market further accelerated. We can see the effort that financial regulatory sectors had put forward in standardizing market system establishment, simplifying administration and decentralizing powers.

Further, a new scientific and technical revolution had been rising, with innovations mushrooming and penetrating various aspects of human society. We had to face such reality actually happening, that productions and consumptions of humans were unprecedentedly being digitalized. Under this irreversible trend, it was possible and necessary to apply technologies to lift the efficiencies of financial risk management and trading. While the nature of finance did not change, methods and means of which would evolve greatly. More and more financial services would extend from tangible physical locations and transform into intangible services embedded in trading and consumption scenarios, reaching every tiny unit, the meaning of which was not negligible for MSMEs financial services.

‘Internet Finance’ had been in the middle of a whirlwind for the past few years, with new types of financial institutions embedded with ‘Internet Genes’ rising strong, P2P lending platforms, true or disguised as, flourishing everywhere, and traditional financial institutions’ attitude toward which changing from ‘almost ignoring’, to ‘participating in discussion’, or even to ‘trying to set foot in’. From herding to aura fading, unpractical expectation had been transforming. Both traditional and new institutions had become more down-to-earth. In 2015, we witnessed elephant-like traditional financial institutions, especially represented by commercial banks, turning around indeed, more proactively seeking cross-boarder cooperation with internet enterprises good at new technologies like cloud-computing, big data and mobile payment, mutually building new financial ecology; while new financial institutions turned to more pragmatic exploration from high-profile propaganda, trying to cooperate with traditional financial institutions with advantages in offline businesses.

It was also the ‘rational recovery’ case for industries like micro-credit companies and pawnshops, whose major customer groups were MSMEs. Industrial recessions had given rise to all-round reflection, concepts like ‘Micro credit should be micro, rather than big’, ‘Pawn should be back to origin’, which could hardly get acknowledgement during prosperity period, had gradually become industrial consensus. Re-identifying market orientation facilitating sustained development, allowing full play to own advantages, and seeking truly differentiated competition with mainstream financial institutions, had turned into challenges that could not be escaped by those industries. We expect more rational recoveries, so that institutions truly serving MSMEs could be distinguished after waves and tides, and those under the banner of ‘inclusive finance’ but not doing the job would find it impossible to disguise.

It is the eighth year for this annual report. The core team set higher requirements on depth of study on the basis of continuously upholding the principle of “objective, neutral and precise”. The commercial bank team carried out the fourth Questionnaire Survey of MSE Financial Managers in Commercial Banks, the number of managers climbed year by year, while regional coverage also enlarged; the rural finance team stepped deep into poor villages and managed to form a more profound understanding of the pain points of rural finance. Particularly, the stock market team and bond market team for the first time tried classifying enterprises in the two markets, in an effort to show the real situation of big-medium-small-micro enterprises financing from capital market, and further objectively demonstrate the changes the development of multi-level capital market had brought about. Though, to some extent, boring, tough, and in need of considerable patience, we did address such basic work as how the worth of our report stood out, utilizing fact and data to show the real situation of China MSME finance and seek broader consensus.

Frankly speaking, there have been both joy and pity looking back at the 8 years. For example, the number of MSMEs taking loans emphasized by our team has been adopted by the authority since 2015 as one monitoring indicator of MSME finance, while SME collective bond, which was followed and studied by our team for years and proved impracticable, still repeatedly appeared in the policies seeking to promote MSME finance. That made us aware that the mission of this report was far from accomplishment.

It is our fortune to have so many fellows, and receive selfless help from practitioners at the frontline and experts and scholars of the industry throughout our writing process, especially our old and new friends acting as our industry expert reviewers, they spared no effort to share their pertinent opinions so that our work advanced with solid ground. Taking this opportunity, we would like to extend our deep appreciation!

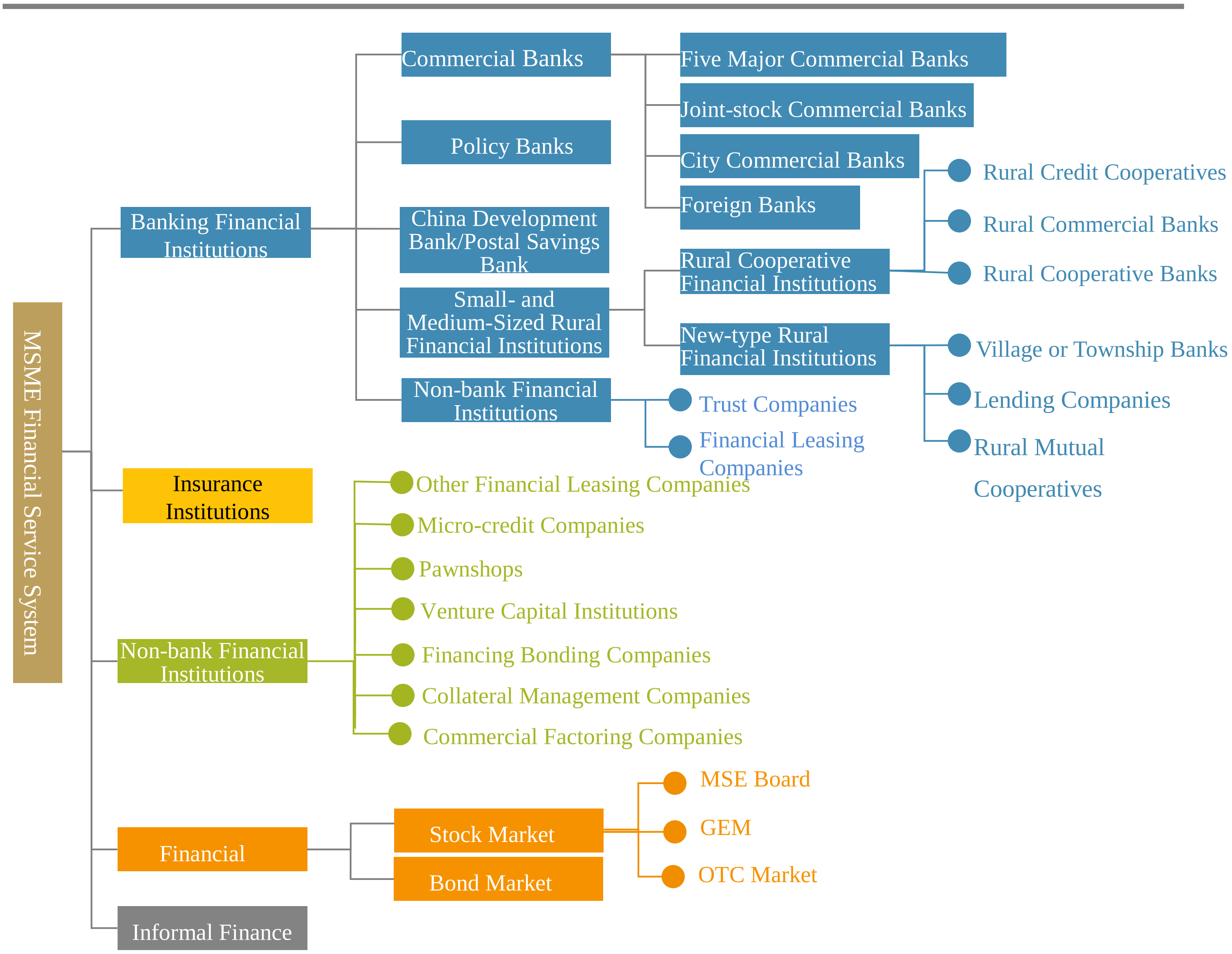
Besides, we would like to thank the publishing team, including Director Wang Xiaorui and Editor Zhang Chao from China Financial Publishing House, for their full support. Their professional spirits and effective execution made it possible that the annual report could reach our readers with best quality and fastest speed.

Last but not the least, special gratitude should be expressed to the readers. There had been calls and Weixin public platform messages inquiring publishing time since the end of June. Sorry to keep you waiting. With higher requirement on depth of the report, tougher tasks in data collection and mining, it took much more time and effort to finish this year’s report. It would be our great pleasure to gain your recognition with our perseverance and endeavor. Welcome to follow ‘mintaijinrong’ Weixin public number, and leave precious comments and suggestions.

1 Micro, Small and Medium Enterprise (MSME) Financial Service System

In this report, MSME financial service system[1] is divided into five categories: banking financial institutions, insurance institutions, other quasi-financial institutions, financial market and informal finance (See fig. 1-1).

Fig 1-1 MSME Financial Service System



1 Generalized MSE financial service system includes not only institutions and market, but also other related intermediaries and environment. In order to highlight the important points of the report, here the system only covers major institutions and market.

Among banking institutions, those involved in MSME financial services include policy banks and China Development Bank, Postal Savings Bank, large commercial banks, joint-stock commercial banks, city commercial banks, foreign banks, small and medium-sized rural financial institutions as well as non-bank financial institutions, hereinto, small and medium-sized rural financial institutions can be further divided into rural cooperative financial institutions and new-type rural financial institutions. Rural cooperative financial institutions include rural credit cooperatives, rural corporative banks and rural commercial banks; new-type rural financial institutions are comprised of village or township banks (VTBs), lending companies and rural mutual cooperatives. In non-bank financial institutions, organizations involved in MSE financial services mainly include trust companies and financial leasing companies.

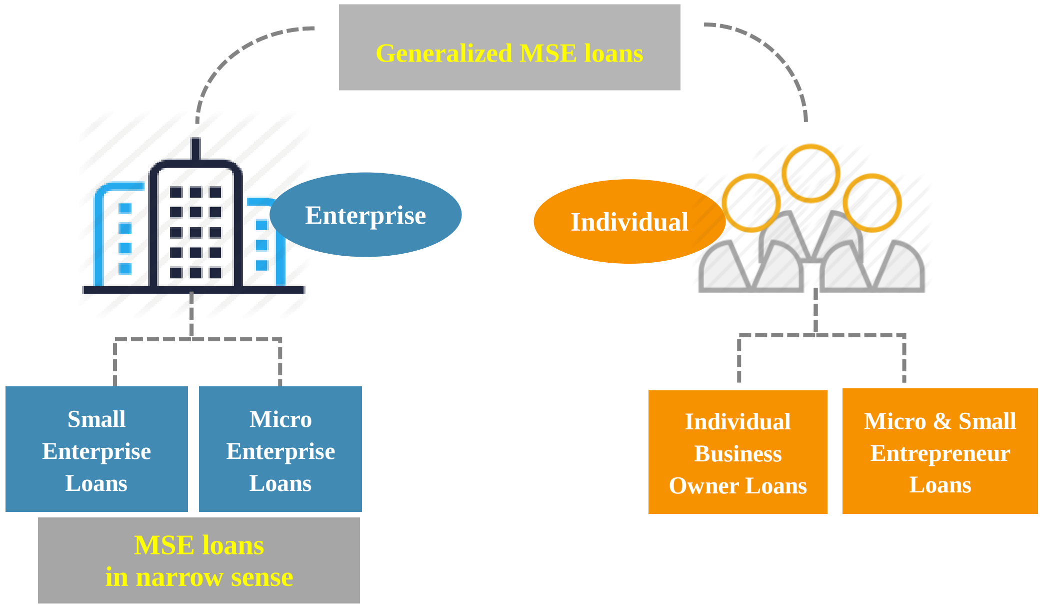
Apart from banking financial institutions, other quasi-financial institutions[1] involved in MSE financial services include micro-credit companies, pawnshops, venture capital institutions, financial bonding companies, collateral management companies, commercial factoring companies and other financial leasing companies. Financial market consists of stock market and bond market, hereinto, stock market comprised Growth Enterprise Market (GEM) board, Small and Medium Enterprise board, and Over-The-Counter (OTC) market. In addition, informal finance covers financial service forms other than formal finance. Finally, other than institutions providing financing services, we also shed light on insurance institutions, which, though do not directly serve financing, provide risk management services.

2 Compositions of MSE Loan Types

Among MSMEs financial services, loan service is one of the major types. In pace with the practical development of MSEs financial services provided by financial services, especially commercial banks, compositions of MSE loan types are further specified. The summary and definition of our team are as follows, generalized MSE loans can formally be divided into two types, one incorporates MSE loans offered through the form of enterprise loans, namely, small enterprise loans and micro enterprise loans (collectively referred to as MSE loans in narrow sense), while the other consists of loans to individual business owners and loans to MSE owners, both offered through the form of personal loans (See fig. 2-1).

1 Though not defined as financial institutions by laws or regulations, these organizations are called quasi-financial institutions due to the financial features of their businesses. In Oct, 2015, *Provisions on Financial Enterprises Classification Standard*, issued by People's Bank of China, China Banking Regulatory Commission, China Securities Regulatory Commission, China Insurance Regulatory Commission and National Bureau of Statistics, classified institutions like micro-credit companies, pawnshops and financing bonding companies as non-monetary-banking service financial enterprises.

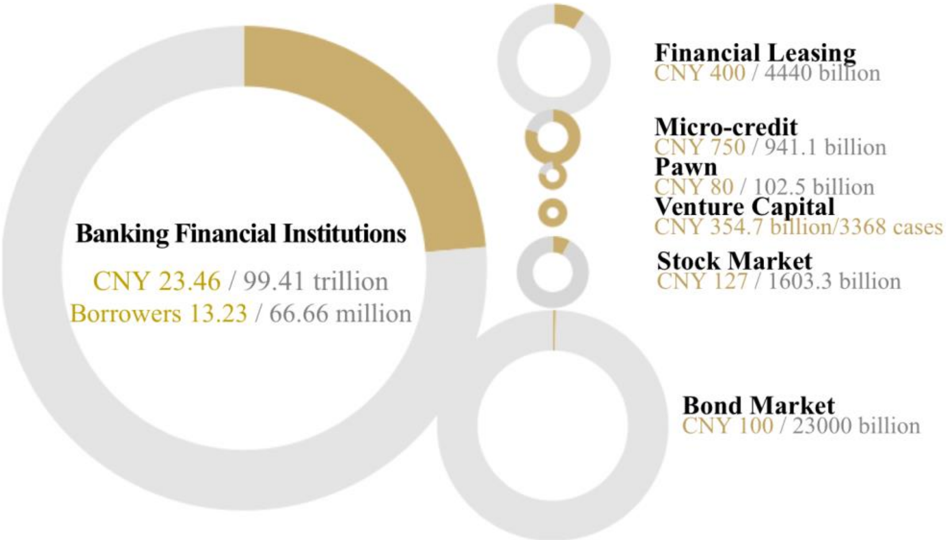
Fig 2-1 Compositions of Banking Financial Institutions' MSE loan types



3. An Overview of MSME Financial Services

Fig. 3-1 shows the scale of MSME financial services provided by major supply agents in the MSME financial service system. We can see that banking financial institutions were still the biggest funds suppliers of MSMEs, providing financing at the scale of trillion for tens of millions of MSEs; those providing financing at the scale of one hundred billion include micro-credit companies, financial leasing companies, venture capital investment, stock and bond markets; the balance of MSME pawn still had not reached one hundred billion. In comparison with that in 2014, there had been little growth in scales of micro-credit and pawn; venture capital investment increased most significantly; while the scales of stock and bond markets embraced a rapid growth, the proportions that did flow to MSMEs were very limited.

Fig 3-1 An Overview of MSME Financial Services（2015）



Note: ①Circles above refers to outstanding financing scales of various kinds of institutions in banking, financial leasing, micro-credit and pawn industries in 2015, hereinto the yellow parts represent outstanding financing scales of MSMEs (gray numbers represent overall scales, yellow ones refer to MSMEs'). Detailed statistical coverage is as follows: for banking financial institutions and micro-credit companies, the statistics/estimation covers generalized MSE loan balances (including small enterprises loans, micro enterprises loans, loans to individual business owners and personal business loans to MSE owners); the coverage of financial leasing and pawning is the MSME loan balances; for venture capital investment, the circle stands for financing increment in 2015, the two yellow numbers respectively represent the investment amount and number of investment cases already disclosed, and the actual scale shall be larger than the disclosed data; for stock market and bond market, the circles represent the financing increment of the two markets in 2015, hereinto the yellow part represent the financing amount of MSMEs (grey numbers represent overall amount, yellow ones refer to MSMEs').
②By the end of 2015, banking financial institutions had provided MSE loan services to 13.226 million MSEs, accounting approximately for 19.8% of the total 66.66 million MSEs nation-widely.

3.1 Banking Financial Institutions

In 2015, commercial banks' overall business environment became more complicated, with operating pressure rising continuously. In context of China's economy entering L-shaped developing period and market competition becoming increasingly fierce, both the gliding of the overall profit level of banking industry and the accumulation of risks urged banks to seek breakthroughs in predicament. The result of our annual Questionnaire Survey of MSE Financial Managers in Commercial Banks[1] showed that, commercial banks' performances in MSE financial services in 2015 were not satisfying. 'Barely satisfactory' and 'Risk aggravating' were mostly mentioned key words by managers, while 'Strict risk control' was the major element considered when providing MSE financial services. Though seeking transformation and

1 For details of the survey, please refer to the annex of the Chinese version: Questionnaire Survey of MSE Financial Managers in Commercial Banks (2016)

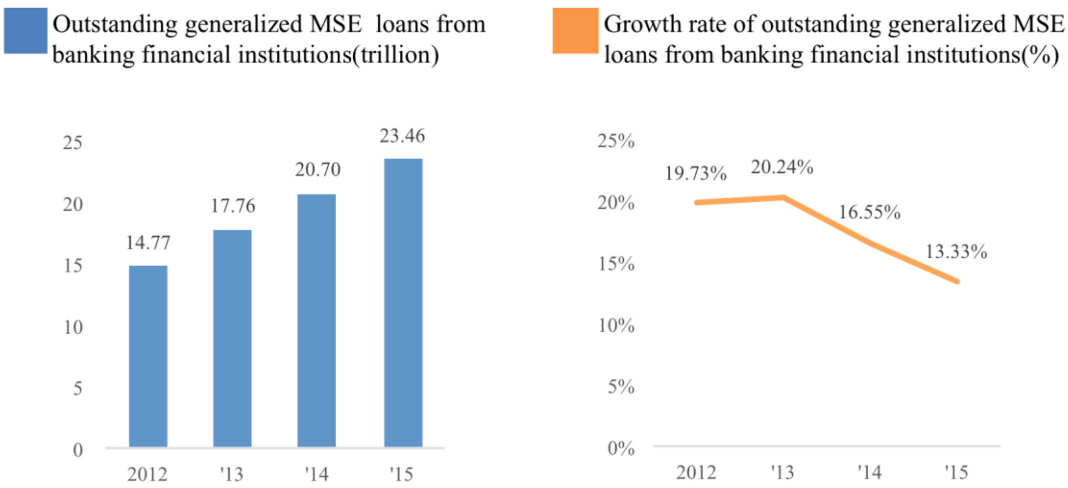
innovation, there seemed ‘a lack of innovation’ generally for commercial banks, ‘progressing hard’ in fierce market competition. As data showed, the rapid growth trend of MSE loan scale offered by commercial banks had come to an end, with rate of increase dropping at large. Mainly by quota management did banks control gross amount and change directions of increment of loans, thus adjusting credit structure. Many banks just could not reach the requirement of ‘the increase speed of MSE loans not lower than the average of total loans’ in ‘the three not-lowers’ requirement. Negative factors affecting MSEs operating still did not ameliorate, while non-performing loans increased inertially.

At the same time, we witnessed the turning of the elephant-like commercial banks in 2015, which speeded up the pacing of utilizing ‘Internet+’. Commercial banks’ MSE financial services realized the change from simplex loan scale increase to comprehensive strategic deployment. By actively using new technologies, enhancing cooperation with governments, third-part credit referring institutions and Internet enterprises, commercial banks vigorously explored MSE financial service modes, broadened and deepened service scope and contents. MSE finance services began to develop in the direction of innovativeness, diversification and sophistication, in the domain of which appeared diversified competition. The development of some emerging fields also brought new business opportunities to banks.

3.1.1Outstanding MSE loans increasing integrally, though growth rate dropping continuously

According to CBRC data, by the end of 2015, banking financial institutions’ generalized outstanding MSE loans was CNY 23.46 trillion (including small enterprise loans, micro enterprise loans, loans to individual business owners and private business loans to MSE owners; unless specifically noted as MSE loans in narrow sense, the loans mentioned in the following all refer to generalized MSE loans), which was an increase of 13.3% compared with that of 2014, but lower than last year’s increase rate by 3.22 percentage point. The nationwide number of MSEs served by loan services reached 13.226 million, 1.78 million more than that of 2014, which was a 15.6% year-on-year growth and 6.6 percentage point higher, accounting approximately for 19.8% of the total 66.66 million MSEs. Outstanding MSE loans offered by banking financial institutions accounted for 23.6% of the total amount, which was a 0.25 percentage point decrease compared with that of 2014.

Fig 3-2 Balance and Growth Rate of Outstanding Generalized MSE Loans from Banking Financial Institutions（2012~2015）

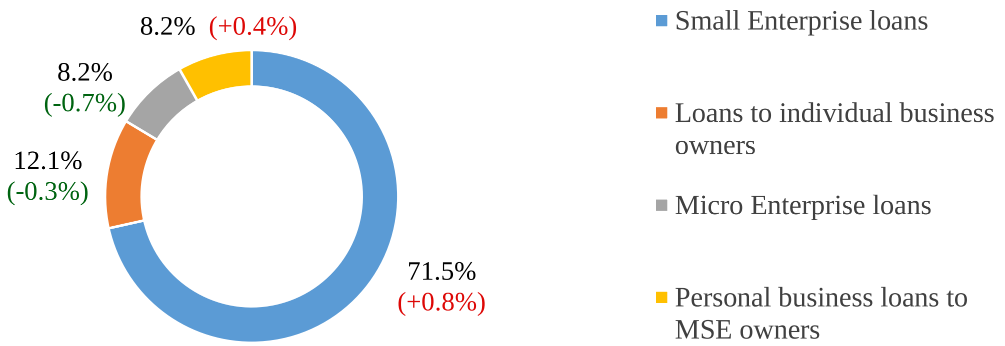


Source：The research team of China MSME Finance Report (2016) from Central University of Finance and Economics summarized the data obtained from CBRC.

3.1.2 Outstanding MSE loans in narrow sense still taking up 80%, while MSE loans offered through the form of personal loans increasing slow

From the perspective of component proportions, 79.7% of outstanding MSE loans from banking financial institutions in 2015 were MSE loans in narrow sense offered through the form of enterprise loans, which went up a bit from 78.6% in 2014. The rest 20.3% were offered through the form of personal loans. Hereinto, small enterprise loans took up the highest proportion, while micro enterprise loans lowest. There were no significant changes in all proportions compared with those in 2014.

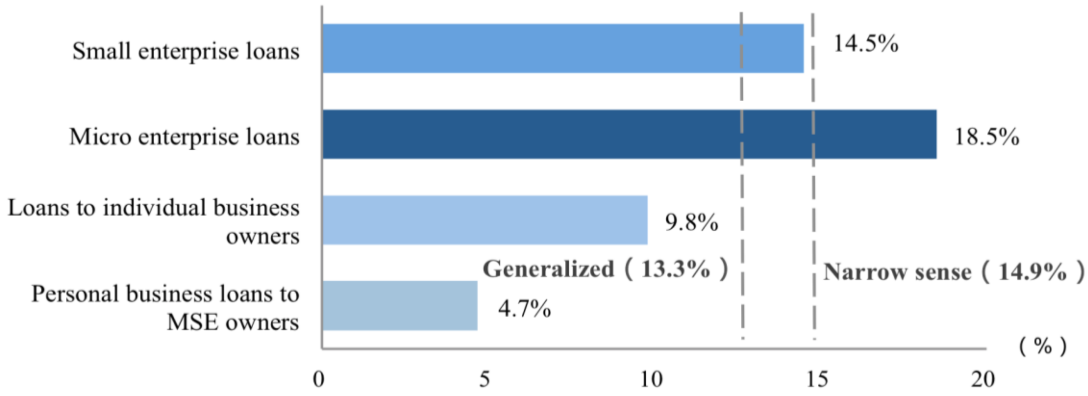
Fig 3-3 Component Proportions of Outstanding Generalized MSE Loans from Banking Financial Institutions (2015)



Source：The research team of China MSME Finance Report (2016) from Central University of Finance and Economics summarized the data obtained from CBRC.
Note: Data in the brackets shows the change of proportions compared with those in 2014.

From fig. 3-4 can we see that, outstanding MSE loans in narrow sense increased 14.9%, higher than the 13.3% increase of outstanding generalized MSE loans. Outstanding MSE loans offered through the form of personal loans were increasing slow, hereinto, personal business loans to MSE owners only increased 4.7%. Among the four types of loans, micro enterprise loans increased the fastest, reaching 18.5%.

Fig 3-4 Growth Rates of Four Types of Outstanding MSE Loans from Banking Financial Institutions (2015)



Source：The research team of China MSME Finance Report (2016) from Central University of Finance and Economics summarized the data obtained from CBRC.
Note: The dotted lines from left to right show respectively the growth rates of outstanding generalized MSE loans and outstanding MSE loans in narrow sense from banking financial institutions.

3.1.3 Five major commercial banks perching at the top of outstanding MSE loans, while rural commercial banks taking 2nd place for the first time

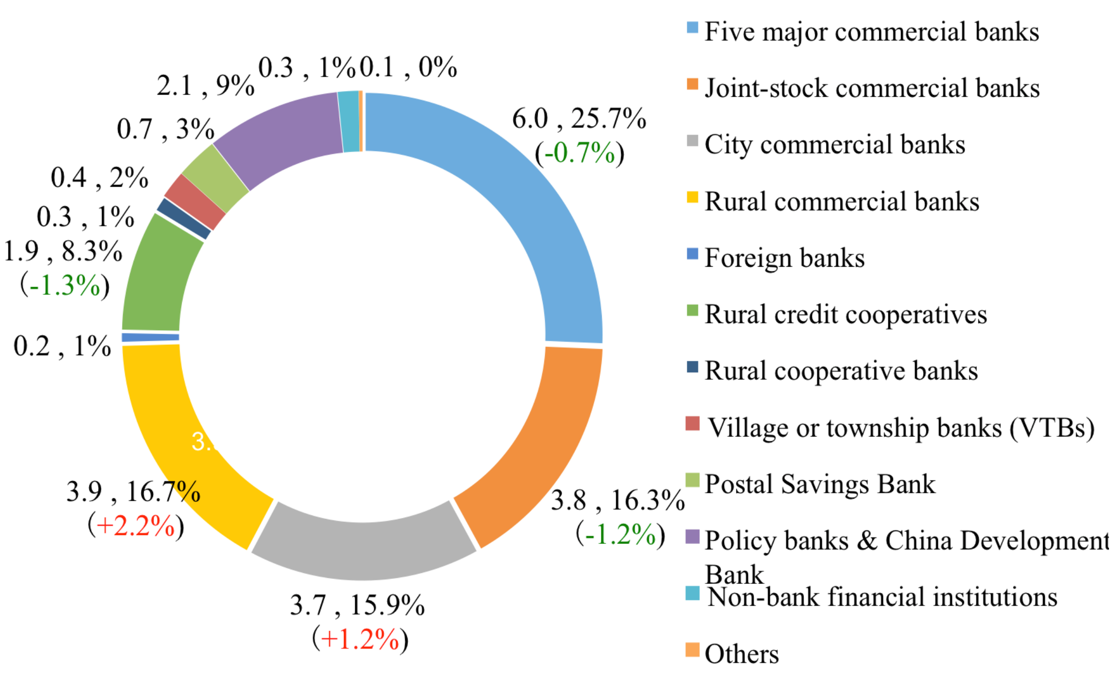
From the perspective of outstanding MSE loans, the five major commercial banks (namely, ICBC, ABC, BOC, CCB, and Bank of Communications) were still perching at the first echelon, taking up 25.7% of all outstanding MSE loans from banking financial institutions with CNY 6 trillion; joint-stock commercial banks, city commercial banks and rural commercial banks constituted the second echelon, outstanding MSE loans of the three types of banks all exceeded CNY 3.5 trillion, accounting for respectively 16.3%, 15.9% and 16.7%.

What’s noteworthy is that, the ranks of outstanding MSE loans of the four types of banks stated above had been along with those of their outstanding gross loans for a long time. Or for simplification, larger scale of gross loans had meant larger scale of MSE loans. Nevertheless, this law was broken in 2015 by rural commercial banks, whose outstanding MSE loans for the first time exceeded those of city commercial banks and joint-stock commercial banks, ranking 2nd place.

The outstanding MSE loans from four types of banks forming first two echelons took up nearly 3/4, while the rest 1/4 were mainly contributed by policy banks and China Development Bank, as well as rural credit cooperatives, the outstanding MSE loans of the two types of institutions were both around CNY 2 trillion, taking up 9.0% and 8.3% respectively.

Compared with the end of 2014, concerning all outstanding MSE loans from banking financial institutions, the proportions offered by the five major commercial banks and joint-stock commercial banks dropped slightly down, those from city commercial banks and rural commercial banks went up, with the biggest increase achieved by rural commercial banks by 2.2 percentage point.

Fig 3-5 Outstanding Generalized MSE Loans and Proportions of various types of banking financial institutions (2015)



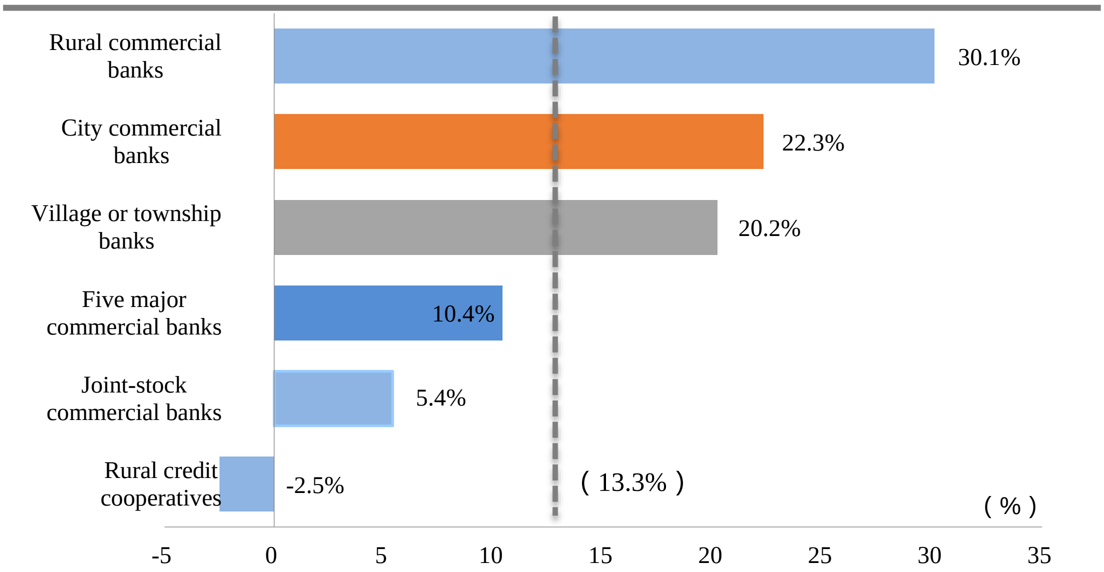
Source：The research team of China MSME Finance Report (2016) from Central University of Finance and Economics summarized the data obtained from CBRC.

Note: Numbers on the left represent outstanding MSE loans (trillion), numbers on the right represent proportions; those in the brackets represent the change of proportions compared with those in 2014.

3.1.4 Growth rate of outstanding MSE loans from joint-stock commercial banks taking the bottom

From the perspective of growth rate, excluding rural credit cooperatives, which had experienced great reduction of institutions due to reorganization, we can see that, growth rate of outstanding MSE loans from joint-stock commercial banks took the bottom, only 5.4%, and the 2nd lowest was 10.4%, from the five major commercial banks. Those from rural commercial banks, city commercial banks and village or township banks kept relatively high, with the highest from rural commercial banks, achieving 30.1%.

Fig 3-6 Growth Rates of Outstanding MSE Loans from Various Types of Banking Financial Institutions (2015)

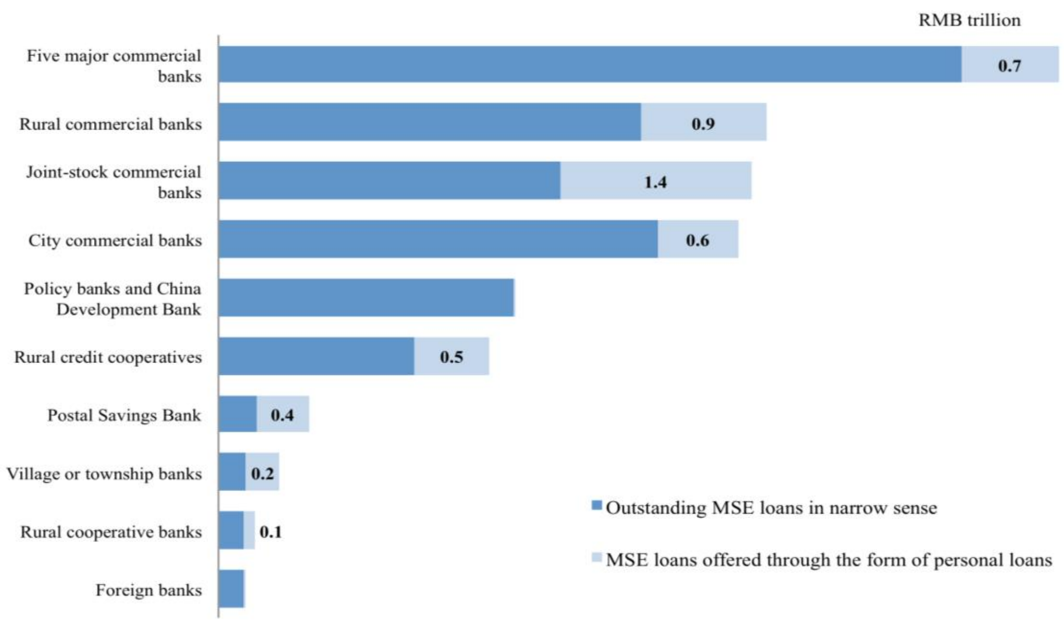


Source：The research team of China MSME Finance Report (2016) from Central University of Finance and Economics summarized the data obtained from CBRC.
Note: ①Due to lack of data for some types of institutions, the comparison above only include institutions whose data of recent two years can be accessed.
②The dotted line above shows that the growth rate of outstanding generalized MSE loans from banking financial institutions was 13.3%.

3.1.5 Structures of MSE loans of various types of banks showing significant distinctions

From the perspective of ranks of outstanding loans, the five major commercial banks took the top regardless of loans generalized or in narrow sense. Other than city commercial banks, all other banking financial institutions took the same places when ranked according to outstanding MSE loans generalized or in the narrow sense. City commercial banks ranked 4th concerning outstanding generalized MSE loans, but in narrow sense, their outstanding MSE loans exceeded those of rural commercial banks and joint-stock commercial banks.

Fig 3-7 Outstanding Generalized MSE Loans and Those in Narrow Sense from Various Types of Banking Financial Institutions (2015)



Source：The research team of China MSME Finance Report (2016) from Central University of Finance and Economics summarized the data obtained from CBRC.

Observing the proportions of the four types of outstanding MSE loans from various banking financial institutions, we can see more standout differences, which also reflected their different customer orientations concerning MSE loans.

For the five major commercial banks, the proportion of outstanding small enterprise loans in all MSE loans achieved 82.9%, higher than that of any type of banking financial institutions other than foreign banks; while outstanding micro enterprise loans only accounted for 5.5%, lowest among all banking financial institutions; outstanding MSE loans offered through the form of personal loans accounted for only approximately 10%.

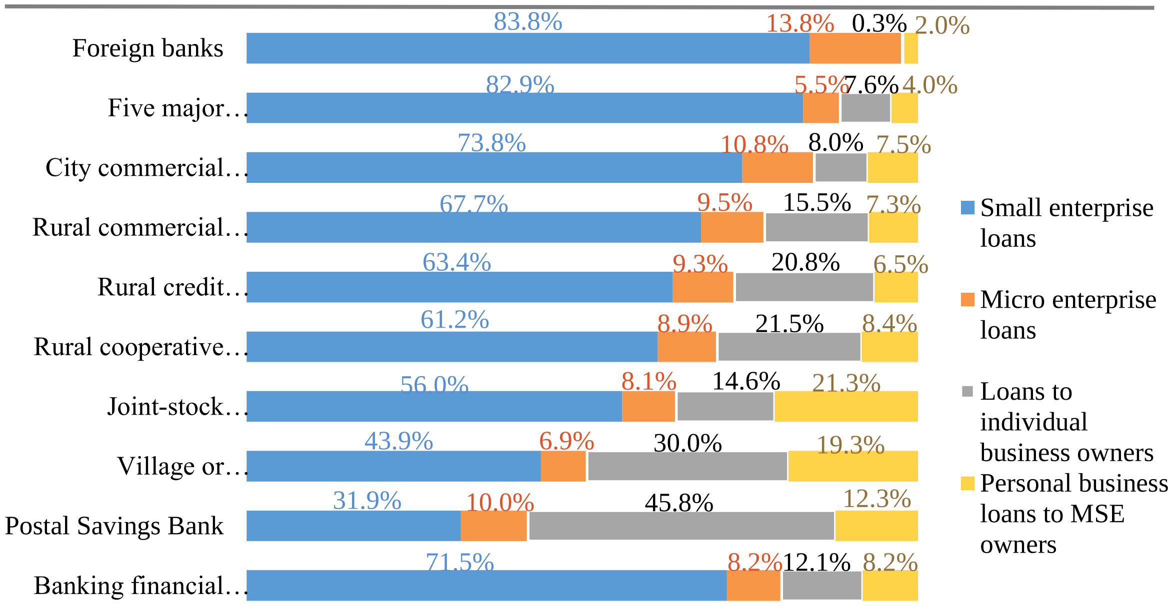
For joint-stock commercial banks, the proportion of outstanding personal business loans to MSE owners accounted for 21.3%, higher than that of any other type of banking financial institutions, nearly accounting for half of all outstanding personal business loans to MSE owners from banking financial institutions; while outstanding small enterprise loans took up only approximately 50%, lower than the average level of banking financial institutions.

For foreign banks, outstanding small enterprise loans accounted for 83.8%; outstanding micro enterprise loans accounted for 13.8%, highest among all banking financial institutions; while there were few outstanding loans to individual business owners from foreign banks, and outstanding personal business loans to MSE owners took up only 2.0%, far lower than that of any other type of banking financial institutions.

For Postal Savings Bank, the proportion of outstanding loans to individual business owners achieved 45.8%, higher than that of any other type of banking financial institutions; MSE loans offered through the form of personal loans accounted for more than half; while its small enterprise loans took up only approximately 30%, lowest among all banking financial institutions.

For rural credit cooperatives, rural cooperative banks and village or township banks, the proportion of outstanding loans to individual business owners were relatively high, while outstanding small business loans took up relatively low proportion.

Fig 3-8 Structures of outstanding MSE loans from various types of banking financial institutions (2015)



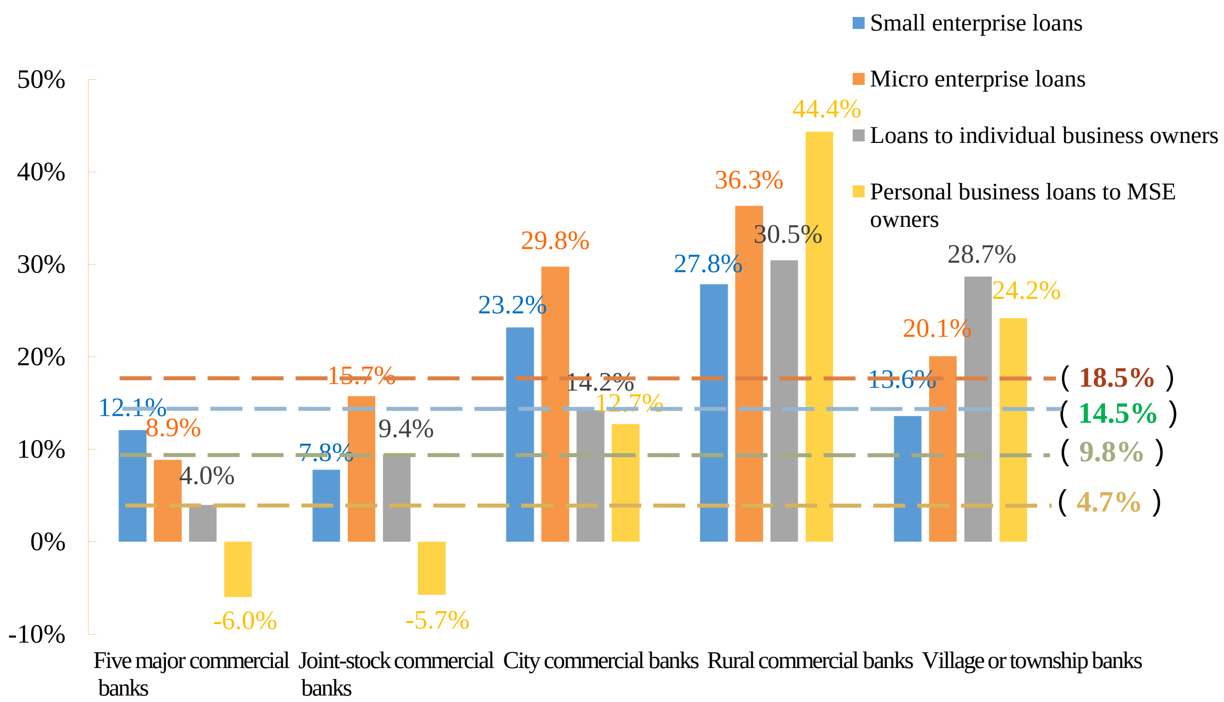
Source：The research team of China MSME Finance Report (2016) from Central University of Finance and Economics summarized the data obtained from CBRC.

3.1.6 Growth rates of four types of outstanding MSE loans from various banking financial institutions showing diversities

From growth rates of four types of outstanding MSE loans offered by various institutions, we can see that different efforts had been paid to different types of loans.

For rural commercial banks, growth rates of four types of outstanding MSE loans from were all higher than those from any other type of institutions, among which the growth rate of personal business loans to MSE owners stood out, achieving as high as 44.4%. For city commercial banks, growth rates of outstanding micro enterprise loans and small enterprise loans were relatively higher than those of the other two types of loans. Oppositely, for village or township banks, growth rates of outstanding loans to individual business owners and personal business loans to MSE owners were relatively higher than those of the other two types of loans. What's worth noting is that, growth rates of personal business loans to MSE owners appeared negative for both the five major commercial banks and joint-stock commercial banks, while those of the other three types of loans were also relatively low.

Fig 3-9 Growth Rates of Outstanding MSE Loans from Various Types of Banking Financial Institutions (2015)

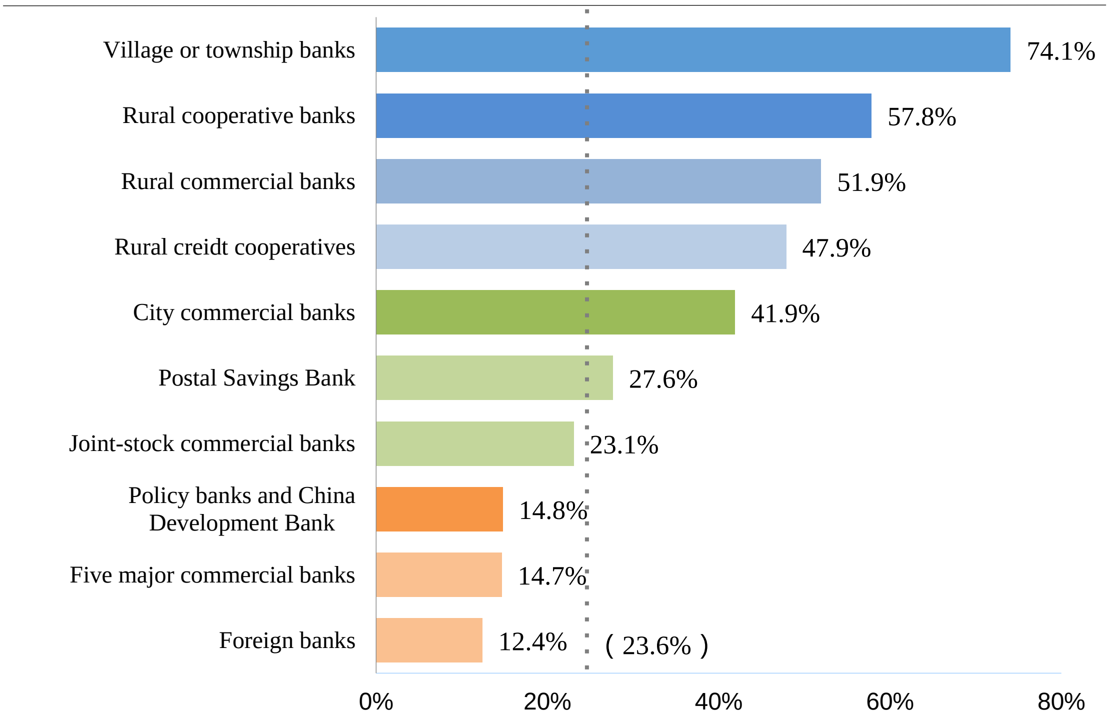


Source：The research team of China MSME Finance Report (2016) from Central University of Finance and Economics summarized the data obtained from CBRC.

3.1.7Rural financial institutions' proportions of outstanding MSE loans in gross loans generally higher than those of other institutions

From the persepctive of proportion of outstanding MSE loans in gross loans, the average level of banking financial institutions was 23.6%. It is noteworthy that, for rural financial institutions (including rural commercial banks, rural credit cooperatives, rural cooperative banks and village or township banks), proportions were generally higher than those of other institutions, hereinto, for village or township banks, outstanding MSE loans accounted for as high as 74.1%; for rural commercial banks and rural cooperative banks, proportions also exceeded half. For five major commercial banks, foreign banks, policy banks and China Development Bank, proportions were respectively 14.7%, 12.4%, 14.8%, far lower than the average level of banking financial institutions.

Fig 3-10 Proportions of Outstanding Generalized MSE Loans in Gross Loans from Various Types of Banking Financial Institutions (2015)



Source：The research team of China MSME Finance Report (2016) from Central University of Finance and Economics summarized the data obtained from PBC and CBRC.

Note: ① Outstanding gross loans from five major commercial banks were summarized from data released by PBC and the annual report of Bank of Communications; outstanding gross loans from joint-stock commercial banks were calculated from outstanding NPLs & NPLs ratio released by CBRC; outstanding gross loans from other types of institutions were from data provided by PBC.

② The dotted line above shows that the proportion of outstanding generalized MSE loans in gross loans from banking financial institutions was 23.6%.

3.2 Other Financial Institutions/ Quasi Financial Institutions

3.2.1Micro-credit companies: the receding tide incurring reflection

After five years' rapid growth, growth rate had begun to go down for micro-credit industry since 2014, which was more obvious in 2015, with growth rates of number of institutions, paid-in capital and outstanding loans for the first time falling back to single digits, outstanding loans even began to decrease. Until of the end of 2015, the number of micro-credit companies was 8910, only 119 more than that of 2014, a 1.4% increase on year-on-year basis, which was a 10.8-percentage-point fall of growth rate from last year. The paid-in capital was CNY 845.93 billion, a 2.1% increase on year-on-year basis, which was a 14-percentage-point fall of growth rate from last year.

Outstanding loans was CNY 941.15 billion[1], a 0.09% fall on year-on-year basis, which was a 15.1-percentage-point fall of growth rate from last year. That was the first time that outstanding loans decreased since trials began.

Micro-credit industry moved on under the pressure of economic downturn, with risks emerging, effective demand decreasing, volume of business and profitability index generally falling, the difficult situation of 'NPLs rising high, new businesses hard to develop, operating performances going down, stockholders losing confidence' widely appeared, the receding tide of micro-credit fever incurred all around reflection on this industry. Warnings like 'Micro credit should be micro, rather than big', which could hardly get acknowledgement during prosperity period, had gradually become industrial consensus with current practical verification. Finding the market orientation promoting sustainable development, fully exerting advantages, forming truly diversified competition with traditional financial institutions, had become the challenges micro-credit industry had to face up to.

Though growing integrally with gloomy outlook, there were still highlighters for the industry in 2015: micro-credit companies were officially classified as non-monetary-banking service financial enterprises, which solved the long-standing identity problem; micro-credit companies started asset securitization and going on the new OTC market one after another to explore new financing channels; local governments release policies to encourage and regulate the development of the industry, in an effort to promoting its sustainable and sound development.

3.2.2 Pawnshops：orienting clearly and back to origin

Until the end of 2015, there were 8085 pawnshops[2] across the country, a 6.7% increase compared with last year, which was also a 4.1-percentage-point fall of growth rate, ending the two-digit increase three years in a row since 2012. Throughout the year, there had been CNY 367.2 billion traded, integrally slightly down from last year, however, the growth rate jumped from cliff, from over 20.0% in 2012 and 2013, to 10.6% in 2014, and in 2015, it fell to -0.5%. There was CNY 102.5 billion outstanding, which was just a 1.2% increase, and also a tumbling decrease of growth rate, 15.7% lower than that of last year.

In 2015, risks occurred frequently in pawn industry, though superficially it seemed that impacts had mainly come from economic downturn and defaults caused by difficulties of enterprise cash flow turnover, but as a matter of fact, pawn defaults caused by MSEs or individuals could not have brought so hard a hit to the industry. Since real estate pawn once accounted for half of the industry's businesses, on the background of real estate market changing momentum of development, related pawn

1 Source：People' s Bank of China。

2 Source: The Pawn Industry Supervision and Management Information System.

businesses, which were usually large in volume, suffered a lot. Besides, with accelerated progress of interest rate marketization, commercial banks paid more attention to MSMEs, along with competitive pressure brought by institutions like micro-credit companies, crowding out MSE demand for pawn financing. To keep customers, the industry had to cut interest and commission rate, which would no doubt affect profitability.

Financial authority of China clarified the identity and status of pawn industry in 2015. Market share of personal estate pawn went up year by year, while traditional goods pawn, which was the foundation of the industry, also won more importance. On the other hand, related policies also encouraged pawn industry to innovate business models with the help of Internet, and at the same time reinforce advantages to serve MSMEs.

3.2.3Financial leasing: hidden worries rising behind high growth rate

In 2015, the development of financial leasing industry kept blooming, with the drive of foreign-invested leasing enterprises, the growth rates of both numbers of financial leasing companies and registered capital exceeded 100%. Till the end of 2015, the total number of financial leasing companies across the country reached 4508, 104.7% more than a year earlier; registered capital of the industry reached CNY 1.52 trillion, 129.4% more than a year earlier. However, rapid growth mentioned above did not go along with leasing business volumes. In 2015, outstanding gross contract of financial leasing companies was CNY 4.44 trillion, just a 38.8% increase. 'Empty-shell' problem still existed in the industry, the appearances of many foreign-invested leasing enterprises were aimed at cross-border capital arbitrage and obtaining government subsidies through overseas loan under domestic guarantee, in which case there would be few real businesses, and foreign-invested leasing enterprises became empty shells. The 20%/80% differentiation of business types was very obvious in financial leasing industry, with the ratio of direct leasing businesses and leaseback businesses once even reaching 1:9.

Affected by macro economic downturn and structural reform, financial leasing companies generally adjusted proportion of businesses to control risk in 2015, and carried out more serious screening of customers, as a result, MSME financial leasing was faced with the challenge of economic downturn, which, however, also indicated that there was still a lot of room for improvement for financial leasing companies to serve MSMEs. At the same time, impact and infiltration brought by the Internet deepened further.

3.2.4 bonding and factoring companies: right time to fix chaos and optimize regulations

In 2015, bonding companies developed under the dual pressures of external economic downturn and internal industrial renovation. Outstanding balance of financing guarantee slowed down, while compensatory amount and ratio rose up. The number of financing bonding companies continued to reduce to around 7300 in 2015, while newly increased compensatory amount was CNY 41.5 billion, with outstanding compensatory amount reaching 66.1 billion at the end of year, a 59.3% year-on-year growth. Policies guiding bonding companies back to origin were more explicit. The introduction of *Proposals on Speeding Up the Development of Financing Guarantee Industry* made it unequivocal that, both financial guarantee businesses, that provided inclusive services for MSEs, agriculture, farmers and rural areas, and re-guarantee businesses, have the attribute of quasi-public goods, which was good for reconstruction of industrial orders, and to some extent suppressing the phenomenon of financing bonding companies not acting out under the banner of ‘serving MSEs, agriculture, farmers and rural areas’. There was hope that the industry could trim numbers and improve quality in virtue of new policies, and resorted to a well-organized and regulated way of development led by policy-oriented financing guarantee institutions.

Though not so prosperous as before, the development of collateral management industry could be further standardized and industrial image be reconstructed with the introduction of *Third-party Management Practices of Guarantee Inventory* and the online operation of ‘Public Information Platform for National Guarantee Inventory Management’. With the strong support of government, commercial factoring industry would embrace important opportunity period by leveraging asset securitization and development of Internet finance. In 2015, main indicators, like the numbers of new commercial factoring companies, volume of factoring businesses and outstanding balance, all kept in the trend of multiplied growth three years in a row. At the end of 2015, there were 2514 commercial factoring companies registered, a 106.1% increase than last year; hereinto, 1294 companies were founded in 2015, a 43.9% increase than last year. The business volume of commercial factoring was CNY 200 billion in 2015, 1.5 times more than that of last year. Till 2015, 500 commercial factoring companies already established had provided service for around 31500 SMEs, becoming one of important channels of MSME financing[1].

3.2.5 Venture capital: accelerated growth with mingled hope and fear

In 2015, influenced by the policy incentive of ‘Public Business Innovation’ and relatively loose currency liquidity, capital poured into venture capital industry, raising an unprecedented wave of start-ups in Chinese history. The activeness of funds financing, investing and exiting kept high in venture capital market, with several data refreshing historic record. Throughout the year, domestic and foreign venture capital institutions raised 721 new funds, increasing CNY 220 billion that could be invested in Mainland China, respectively 142.76% and 78.00% higher than last year, hereinto,

1 Source: ’The Development Report of Commercial Factoring Industry of China 2015’.

the growth of angel funds was particularly impressive. Besides, government-led funds experienced spurt-like growth, exceeding 1 trillion in scale. Both the number of investment cases and investment amount increased massively, there were 3368 investment cases, relating CNY 354.69 billion around the year, respectively 86.7% and 81.95% higher than last year. What was particularly surprising was that, those two indicators above even doubled for angel funds. In 2015, there were totally 1813 exiting cases in 2015, 4.09 times that in 2014, hereinto, those from the new OTC market accounted for half the deals, from which the added carrying value effect promoted great zeal toward venture capital investment. With the background of adequate venture capital supply, it became much easier for start-ups with innovation capability to find access to financing than before, while the amount of funds acquired by them also increased significantly together with valuation level. Meanwhile, it was not ignorable that, ‘patient’ capital and professional investors were relatively scarce and valuation levels were virtually high, leading to trend-following phenomenon where many start-ups lived short. Consequently, calls for the industry to be back to professionalism and rationality gradually rose.

3.3 Financial Markets

3.3.1 Stock market: deepened development of multi-level market

It was a rollercoaster-like year for A-share market of China in 2015, going from fiery fast bull market to icy crash. From the perspective of market structure, development of multi-level stock market further deepened, finance from MSE board and GEM tended to be more rational and diversified, stock transfer system enlarged rapidly, pattern of ‘one OTC market for one province’ stood out, and the foundation of multi-level capital market became solid gradually. From the perspective of equity financing, the phenomena of IPO over-raising were restrained, SEOs turned dominant, and financing methods became more diversified. In 2015, there were totally 2742 enterprises financed through the main board, MSE board, GEM and stock transfer system, 209.48% higher than 886 enterprises in 2014; aggregate financing amount was CNY 1.6 trillion, 60.29% higher than 1 trillion in 2014.

Though the multi-level market was becoming increasingly strengthened and financing amount was growing continuously, large and medium enterprises were still the main service targets of stock market, homogenization was evident in the floor trading market. From the perspective of firm size structure, there were no distinctions among MSE board, GEM or the Main Board, leading to the loss of meaningfulness for board names, which might be the result of Shanghai and Shenzhen stock exchange markets fighting for IPO resources, as well as the arbitrary choices of enterprises in the queue for IPO. From the perspective of financing amount, majority flew to large enterprises in stock exchange market in 2015, and amount acquired by MSMEs still appeared inadequate. There were totally 4913 MSMEs listed in stock exchange market in 2015, accounting for 61.92%, while financing amount was CNY 127.04 billion, accounting for only 7.92%. How to, bit by bit, connect the services provided by capital markets on the basis of multi-level market, with the financial demand of the real economy, how to achieve further optimization and resource integration of internal structure of multi-level capital market, would be important subjects in need of consideration in the future.

3.3.2 Bond market: policies giving way to marketization

In 2015, bond market continued to advance triumphantly with CNY 23.19 trillion financing amount, 90.26% higher than last year. China Bond Aggregate Wealth (Gross Value) Index increased 8.03% throughout the year; 10-year treasury yield went down from 3.63% at the beginning to below 3% at the end of the year. Corresponding to the overall downward of yields in secondary bond market, coupon rates of newly issued bonds decreased evidently, which reduced bond financing cost for enterprises, and promoted expanding of enterprise bond financing scale.

In the primary market, various types of newly issued bonds by non-financial enterprises achieved CNY 6.82 trillion in 2015, with the net scale of which being CNY 2.94 trillion, respectively 36% and 21% higher than last year. On the other side of bond finance expansion, number of SME concept bonds issued and corresponding financing amount were continuously shrinking, though bond financing by SME issuers up to standards was still active. With the formal promulgation and implementation of *Procedures for Management of Corporate Bond Issuance and Trading*, the range of agents that could issue private placement bonds enlarged remarkably, and the specific term of ‘SME private placement bonds’ gradually faded out. In the context of frequent bond defaults and decreasing risk preferences of investors, the difficulty to directly finance through bond issuance kept rising for SMEs, and there was only symbolic significance for the existence of SME collective note and SME collective bond. It was more noteworthy that, 80% of bond finance by scale explicitly distinguishable SMEs in 2015 flew to comprehensive category (mostly subsidiaries of large holding groups), real estate industry and financial industry, while in industries like manufacturing, wholesale and retail, which were SMEs-rich, there were few, or even no SMEs financing through bond issuance, which to some extent reflected the weak positions of SMEs in traditional industries to finance from bond market.

The good news was that, financing behaviors of small and medium financial institutions in bond market started to demonstrate diversified characteristics, with regional commercial banks still being the main forces for issuance of MSE-specific financial bonds. Rise of asset securitization liquidized credit assets stock of small and medium financial institutions, strengthened their supply capability, and added highlighters to MSME finance in bond market. Generally speaking, in 2015, regarding MSME finance, the trend of policies giving way to marketization continued in bond market.

3.4 Insurance: Heavy Responsibilities to Fulfill, and A Long Way to Go

In 2015, insurance industry of China kept growing rapidly, with total assets of the industry breaking CNY 12 trillion, turning into the 3rd largest insurance market worldwide. Original premium income achieved CNY 2.43 trillion, 20.3% higher than that in 2014, both the premium income and growth rate indicators recorded highest in past five years. With continuous rapid growth of premium income, the industry outshined others regarding the pressure of economic downturn.

However, notwithstanding the government had introduced many policies to promote the development of enterprise-related insurance[1], the market was still growing without strong force, especially MSMEs had rarely taken advantage of insurance. From the perspective of premium income, till the end of 2015, enterprise-related original premium income was CNY 174.2 billion, only 6.6% higher than that in 2014, accounting for 21.8% of property insurance original premium income, and only 7.2% of total original premium income; yet growth rate kept declining, from 24.9% in 2010, sliding to 6.6% in 2015. It should be noted that, the 174.2 billion premium income mentioned above mostly came from large enterprises, due to lack of risk management consciousness, MSMEs had rarely made use of insurance to shift risks. Drived by policies, several provinces had started the trial of micro-credit guarantee insurance, the credit addition mechanism of which could provide more chances for MSEMs to get access to bank loans, an attempt to relieve the difficulty of MSME finance with insurance. But that relied heavily on the drive of government, with not optimistic marketization prospect.

In 2015, Internet insurance realized leap-forward development. Selling traditional insurance products through Internet channels reduced cost, while new types of Internet insurance (MSE insurance, sales return insurance, quality guarantee insurance, etc.) met the need of customers. Application of big data and rapid development of Internet insurance brought new opportunities for insurance industry, and explored new areas for the industry to provide services to MSEMs. On the whole, there were heavy responsibilities to fulfill and a long way to go for insurance to serve MSMEs well.

1 Enterprise-related insurance in this report include property insurance, liability insurance, project insurance, freight insurance, hull insurance, credit insurance, guarantee insurance, special risk insurance, agricultural insurance, excluding insurance for employees (life insurance, accident insurance and health insurance, etc.).

3.5 Informal Finance: various agents vying for new businesses, while regulations sent forth

On the background of economic ‘New Normal’, operation of Chinese economy was still faced with difficulties and challenges. With formal financial system, say banks, squeezing credit, it was even harder for MSMEs to finance. As a consequence, informal finance channels were becoming more important for MSMEs. In the meantime, with the continuous accumulation of private capital, dispersed and petty funds were in the need of extensive and convenient investment channels. Driven by both supply and demand sides, informal finance was becoming increasingly active in 2015, integrally expanding against economic downturn, with number of institutions growing rapidly. In the context of information transmission efficiency increasing steadily, liquidity of private funds rose gradually, economic and interest rate distinctions among different areas motivated informal finance to break through traditional restrictions based on kinship and geography. With the infiltration of Internet, its spatial range was becoming far wider. However, dispute cases related with private lending also happened frequently with the rapid development of informal finance, ranking the 2nd most sued civil cases after marriage and family ones, with financing amount litigated rising every year, rousing extensive concern from various sectors of society.

The introduction of *Supreme People's Court’s Provision on Issues of Applicable Law in Hearing Private Lending Cases* and *Ordinances on Non-deposit Lending Organizations (Draft)*, to some extent, made informal finance once in grey zone start to appear in the sun, unconventional lending between enterprises, or between enterprises and individuals, could then be carried out in reasonable range, and protected by law. That would play an active role in controlling risks of informal finance and enriching financing channels for micro and small agents. However, *Ordinances on Lenders*, on which great expectation was placed, as fundamental law of informal finance, still did not come out, leaving a long way for informal finance to truly operate in the sun.

In 2015, the development of P2P lending industry surged. From the perspective of trading volume, the industry kept in high pace of growth within the year, with historic accumulated volume breaking CNY 1 trillion. Yet behind the industry’s integral barbarian growth arose severe fraud cases and trust crisis, the reversal in 2015 was so acute that the industry’s further development was affected. In the context of slowing economic growth, many P2P platforms were in face of transforming challenges. From the view of policy environment and regulation development, P2P lending was vested with important mission of financial innovation, and high expectations of relieving the difficulties of MSME finance, however, the real effect remained to be checked. Crowdfunding ushered the first big year of development, with number of platforms growing explosively and symbolic turn arising, yet further development of which encountered obstacles. New pilot areas were added in regional reforms of financial system, while representative city Wenzhou kept exporting experience and exposing problems to be solved.

4.Prospect of MSME Finance Development

In 2016, global economic and financial situations were still complex and challenging. During the processes of transformation and upgrading of domestic economy, and transition of old forces of economic growth to new ones, contradictions and risks long accumulated further revealed, while pressure from economic downturn was not ignorable. 2016 was also the beginning year of 13^{th} Five Year Plan. It was put forward clearly by the central government that, in the next period, at the same time of moderately expanding gross demand, the ‘Five Critical Tasks’, namely de-capacity, de-stocking, de-leverage, reducing cost and fixing weaknesses, should be well fulfilled. We shall streamline administration and delegate power to the lower levels, and strengthen regulations at the same time, transforming government functions and raising efficiency, adding on supply of public goods and services. We shall thoroughly implement innovation-drived development strategy, promote deep integration of scientific technologies and economy, transform and upgrade traditional industries, breed and develop burgeoning ones, accelerate the development of modern service industry, improve integral quality and competitiveness of the real economy. We shall boost reform of investment and financing system, develop multi-level capital market, raise the proportion of direct finance, and optimize financing structure. We shall vigorously push forward reform of state-owned enterprises, better stimulate the vigor of non-public sectors of the economy, and facilitate various types of enterprises to pull its weight and realize mutual development. With direction pointed out, the process would be full of challenges; difficulties already met as reform deepened were tougher than expectation.

Under the pressure of economic downturn, both the real economy and financial industry are going through sweeps of ebb tides, ‘that who is skinny dipping cannot be known until tides fall’. During industries’ ups and downs, enterprises, that are both perseverant in doing own jobs well and keeping innovation capabilities with times, would stand out and bring lasting power to the development of the industry. In the meantime, new industries, business modes and growing forces are being bred, and endogenous vigor of some emerging fields is gradually becoming stronger. Those mentioned would all bring new opportunities to MSME finance. In the view of policies, publish and implementation of *Program on Promoting Development of Inclusive Finance (2016~2020)* and *Proposals on Promoting Sound Development of Internet Finance* have set a good tone for MSME finance.

Though ‘controlling risks’ would still be the theme for banking financial institutions, MSME financial service innovations that have started would not stop, and exploring commercially sustainable MSME financial services would still be one of critical directions for transformation of banking industry. Since different institutions have distinct endowments, as well as differed understanding and application ability of new technologies, there could be more diversified competition in this field. Albeit the phenomena of growth rates of MSE loans decreasing, or even to negative, might continue, what can be ensured is that, breadth (number of enterprises served) and depth (diversification of services) of MSME financial service would expand. In such context, the trend that non-mainstream financial institutions like micro-credit companies and pawnshops would come back to origin would be more explicit, industry reshuffle would persist, and structural differentiation would be increasingly evident. In 2016, with the back of adequate liquidity, funds might continue to swarm into financial leasing, factoring and venture capital industries, bringing superficial prosperity, and rational recovery might still be an expectation that could not be fully realized. Nevertheless we could not eliminate the possibility that some farsighted enterprises would step faster in MSME finance, and enlarge their distances with competitors. For insurance industry, there would be a long way to go. Internet insurance products based on industry chain and operation data might break the ice and provide help to risk management of specific type of MSMEs, but the situation that MSME insurance products accounting for low proportion in entire property insurance market would not change fundamentally. Informal finance would continue to be active, yet on the background of macro economic stagnation and private investment demand decreasing, proportion of informal finance that would flew to MSEMs might be affected. What’s worth expectation is that, following the cooling of Internet finance fever, industries have come to the consensus that, data and technology drived risk management, scenarized financial service, and capabilities to extensively connect and reach customers, would be the subjects more and more emphasized by various types of agents serving MSMEs. Cooperation between traditional financial institutions and new-type financial institutions, between traditional financial institutions and non-financial enterprises that possess specific resources, would continue to advance while different types of enterprises running-in, triggering more highlighters of MSME financial service innovation.

Continuous rising of direct finance’s proportion would be of great possibility, while the situation of stock and bond markets mainly serving large and medium-sized enterprises would sustain for a long period, counting on public capital market to finance MSEs is neither realistic nor according with orientation of capital market. Comparatively, that financial disintermediation effect caused by large and medium-sized enterprises’ direct finance through capital market would promote indirect financial system to focus more on lower end and improve MSME finance would be more expectable. Apart from that, it would be hopeful for us to see that more and more agents providing MSME financial services would be able to finance in capital market, commercial banks, factoring companies, micro-credit companies, financial leasing companies, trust companies would engage more in the increasingly hot asset securitization market, securitization products backed by MSME loans, receivables and leasing assets would further increase, which might not become mainstream asset securitization products, but could provide support for MSME capital turnover. That would be a realistic path worth encouraging for capital market to serve MSMEs.