

SECTION 3: The rationale of the choice of managerial problems/ issues

(a) Vision and Mission

SME Bank's vision is to become the SME Hub by 2010 with the unique capability to evaluate, promote and grow Malaysian SMEs with a focus on the development of the Bumiputera Commercial and Industrial Community (BCIC) in line with the Government's aspirations. The Scheme is partially to assist towards this vision by providing support in term of guarantees to the businesses that are viable but do not have sufficient collateral for financing. This will support for their operation's expansions and to boost up the economy.

The mission statement of SME Bank states that in achieving recognition as the SME Hub, the management and employees of the Bank will collaborate with its network of strategic partners/providers to focus on becoming the centre of knowledge and expertise on the financing and growth needs of Malaysian SMEs. The scheme is a tripartite arrangement between Participating Financial Institution, borrower and SME Bank. The credit risk is assumed by SME Bank, whereby the claims need to be settled by SME Bank when there is loan defaulting for amount that guaranteed.

Therefore, rationale of the scheme as the choice is firstly to overcome the increasingly claim ratio, whereby the fee based income fee from this scheme is to support the financing income for SME Bank. This is to ensure that this product is still viable in term of cost and benefit on operations of the scheme.

Secondly, the accumulated claim payment made will reduce the balance available in the Guarantee Reserve Account. The Guarantee Reserve Account is created to back all the Letter of Guarantees issued under the scheme. The balance in the Guarantee Reserve Account determines the Bank's capacity to issue further Letter of Guarantees. The initial sum placed was RM50.0 million and all claims are paid by the Bank are paid out from this account. The bank could only offer lower amount of guarantee to its customers based on the lower available balance in the Guarantee Reserve Account. In summary, the guarantee mechanism adopts multiplier effect, whereby for every Ringgit of reserve the Bank has, the Bank can provide 4 times in loan value to the borrowers.

Thirdly, there is an issue of decrease in number and amount of Credit Guarantee approval, that cause the target is not achieved as per initial plan during introduction of this scheme.

(b) Long term and short term objectives

The long term objective of the Credit Guarantee Scheme is to increase the fee based income for the bank progressively. The higher the approval amount, the higher is the amount of fee based income that can be charged to the customers. The rate is at 1.5% per annum for fee payment made in lump sum and 2.0% per annum if the fee is paid in instalment.

There is an issue of decrease in demand and poor approval on Credit Guarantee for year 2009. The highest approval was 64 approvals amounting RM59.7 million in 2007, and 2 approvals only in 2009 amounting RM1.5 million, whereby this indicates lower fee based income for the Bank that need to be addressed.

Meanwhile, the short term objective is reduce and minimise the claims as far as possible, whereby this will reduce further the operations expenses for SME Bank. Higher claims on the guarantees are not a good indication. For the last 4 years, the claim payment has increased due to the increase of loan guaranteed that becoming non-performing. This issue need to be tackled to ensure that the scheme is still viable.

(c) Competitive analysis

SME Bank does not offer trade lines like commercial banks such as Overdraft, Letter of Credit, Trust Receipt or Bill of Purchase. Therefore, the Bank has to look at overcoming this problem to be more competitive in the market, whereby the Credit Guarantee Scheme comes into plan. The management of SME Bank decides that the Bank will provide the Guarantee Facility, meanwhile CIMB, the strategic partner will provide the Overdraft, Letter of Credit, Trust Receipt or Bill of Purchase lines to the customers.

The target sectors for the scheme such as manufacturing (including agro based) and manufacturing related services, selected services including Information and Communication Technology (ICT), construction and tourism related activities such as hotel resorts and travel agents.

There is an issue whereby the customers that being guaranteed turns bad after certain period of time. There is an issue of viability of the scheme, whereby the claim payment made on guarantee is more than the commission income received by the Bank. The Bank need to be competitive and bring in good customers compare to other financial institutions that offers the similar range of products. To be competitive does not mean to sacrifice the

quality of financing. The requirements of the target sector is something that needs to be explored further.

(d) Product and development

The objective of the scheme initially is to assist businesses that unable to come out with sufficient collateral to get loans from the financial institutions. Since the market in changing throughout time, the scheme needs to be dynamic to suit to the requirements of customers. The continuous improvement should take place to ensure the importance of the scheme to the target market.

The benchmark is response from the public on the scheme. Ideally, higher approval indicates suitability and demand by the customers. However, as indicated that the rate of approval for the scheme is not impressive for past previous years since its first public appearance in year 2006.

(e) Marketing

The marketing is done together between the Participating Financial Institution and SME Bank by capitalising the synergy. SME Bank enables to offer a complete range of facilities to its customers particularly on most commonly requested facilities that SME Bank could not provide namely Overdrafts, Letter of Credit, Trust Receipt and Bill Purchased.

The benefit of this scheme is making use of existing infrastructure of both SME Bank and Participating Financial Institution namely the networking and branches, human capital,

experience and expertise, which will reduce the cost. SME Bank gets the advantage of being able to offer a complete range of facilities and access to fund of the Participating Financial Institution. It provides competitive edge to SME Bank and able to provide flexibility in packaging of financing to customers.

The advantage to Participating Financial Institution is minimum effort as SME Bank will perform financing appraisal, preparation and execution of Facility Letter and perform review. Credit risk is assumed by SME Bank and claims will be paid to the Participating Financial Institution in the event of loan default. Focusing is on the Small and Medium Industries and to strengthen position in this area.

The effectiveness of marketing is usually measured by the number and amount of approval of the scheme. The lower achievement indicates in recent years that require further improvement to be made.

(f) Finance

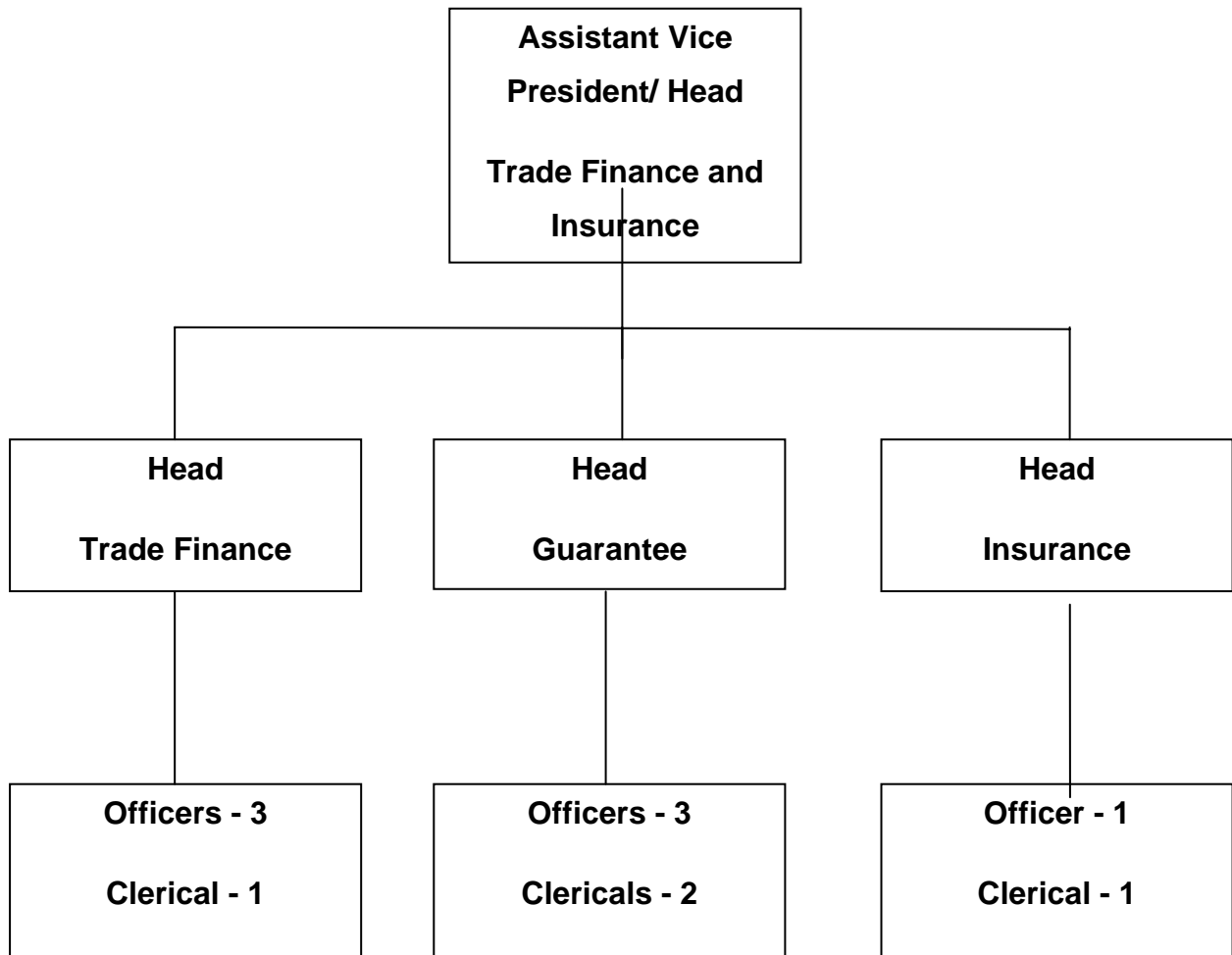
Ideally, the fee-based income generated from the Credit Guarantee Scheme should be higher than the cost. Otherwise, the operation of scheme is financially not viable. There are issues as highlighted earlier such as increase in the loan defaulters that cause higher claim payment and decrease in demand for the scheme that contribute to lower fee based income. These issues have affected the income and profit of the Bank, which requires attention by the management to overcome them.

(g) Organisation and management

The Trade Finance and Insurance Department is entrusted to oversee the implementation of the Credit Guarantee Scheme. The department is headed by Assistant Vice President/

Head and he is supported by 7 officers and 5 clericals. There are 3 sections under this department, namely Guarantee, Trade Finance and Insurance.

The organisations chart of Trade Finance and Insurance Department is described in the diagram below.



The department also handles general insurance for the customers of the Bank. There are 3 officers and 2 clericals that handle specifically on guarantees whereby is currently sufficient.