Loan Guarantee Schemes
Role in Supporting SME Development

The Jordan Case
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The paper aims to clarify the role of the Jordan Loan Guarantee Corporation in supporting SMEs & its vision for developing SMEs sector in Jordan.
Importance of SMEs in Open Economies

- SMEs help provide many job opportunities and contribute greatly to lowering rates of unemployment.
- The reason for this is that SMEs are more Labour Intensive and depend on simple technologies unlike large enterprises that use expensive machines, which in turn increase the cost of job opportunities.
SMEs Contribute Significantly in development and growth which in turn reflects on the economy itself and eventually increase in GNP.

Generally, SMEs represent above 90% of total projects worldwide, and in Jordan they account for around 97%.

As a developing country with limited resources Jordan’s present & past governments have continuously tackled the problems of poverty & unemployment by supporting the SMEs sector.
In addition to the organizational and technical challenges facing SMEs sector, our emphasis on this paper will be on the Financial challenges. These challenges require and demand for proper conditions to SMEs to enable them to obtain their fair share from the financial sources available.

- Financing SMEs in Jordan is provided by subsidized Financial Funds in addition to Commercial Banks and some specialized Financial Companies.
Obtaining financing from traditional financial channels such as commercial banks holds many challenges to SMEs, because:

Banks consider these enterprises a very high risk and hesitate when dealing with them.

Banks consider their main clients the large enterprises with a long financial history without difficulty in providing the necessary financial documentation & collaterals.
Large scale economy plays against SMEs for the internal procedures required by banks to grant a small loan is the same as those required for large ones. They both need complete credit analysis taking the same amount of time & cost, which makes banks abstain from financing SMEs.
Banks when dealing with loan applicants (and they have the right to) require full documentation and proper financial records, which might be difficult for SMEs to provide. Finally, SMEs can’t provide the necessary guarantee (usually real estate guarantee) the banks require from loan applicants. In order to encourage commercial Banks to provide funds to SMEs, Jordan Loan Guarantee Corporation (JLGC) plays a pivotal role to replace the Traditional required real estate collateral.
Central Bank of Jordan (CBJ) Support for JLGC

- In addition to its participation of around 50% of JLGC capital of 10 million Jordan dinar, the Central Bank of Jordan CBJ took practical steps to further encourage commercial Banks to extend loans to SMEs.

- Participating Banks using the services offered by the Jordan Loan Guarantee Corporation have the following privileges from the CBJ:
  - Loan Guaranteed by the JLGC are considered Good loans for which general provisions required by the CBJ are waived throughout the life of the loan. Banks are exempted from allocating special provisions against defaulted loans for the first year of the defaults. However, these provisions are to be allocated for the second year.
  - The portion of the participating bank’s assets of guaranteed loans are considered preferred assets and therefore the Weighted Average of Capital Adequacy required from banks against its loans is decreased.
It is worth noting that some Central Banks in MENA Region took encouraging steps to increase SMEs finance.

For example, the Central Bank of Egypt allowed banks to deduct the volume of loans goes in favor of SMEs from their total deposits when the obligatory reserve requirements is calculated.
The Jordan Loan Guarantee Corporation

Enhancing sustainable economic growth in Jordan through improving the credit environment available to the economically viable small and medium sized enterprises and national exports by providing them with credit and loan guarantees

Since 1994
JLGC started operation, in 1994 with only one program directed towards SMEs. Now, JLGC is operating the following (specialized programs):

I. LOAN GUARANTEE PROGRAMS

- **PRODUCTIVE LOAN GUARANTEE PROGRAM:**
  - Loan Guarantee Program for Small & Medium Size Enterprises (SMEs)
  - Industrial Modernization Loan Guarantee Program-EJADA
  - Leasing Loan Guarantee Program-EJADA
  - Enhanced Productivity Loan Guarantee Program-IRADA
  - Working Capital Loan Guarantee Program

- **Personal Loan Guarantee Programs**
  - Housing Loan Guarantee Program
  - Urban Development Housing Loan Guarantee Program
  - Land Purchase Loan Guarantee Program
  - Computer Loan Guarantee Program

II. CREDIT GUARANTEE PROGRAMS

1. **EXPORT CREDIT GUARANTEE PROGRAM**
2. **DOMESTIC CREDIT GUARANTEE PROGRAM**
The Following analysis will focus on the mechanism followed by JLGC regarding the first program concerning Loan Guarantee Program for SMEs in Jordan.

Objective of the Program:
To assist SMEs owners to establish new projects or expand and improve existing ones to increase the efficiency and income of these projects and to create new job opportunities.
To encourage commercial banks to provide funding for such projects based on their economic viability and cash flow, supported by the guarantee provided by JLGC.

Advantages:
This program covers the risk of funding new projects in addition to those risks related to the expansion and/or the improvements of existing ones.
The program covers the financing risks of all viable income generating projects from different sectors of the economy (industry, professions, agriculture, trade, commerce, services, contracting, construction, and communications).
The possibility of granting a grace period depending on the aim and specification of the project.
The possibility of financing the purchase of fixed assets or working capital or both.
Conditions:
• The maximum amount of loan up to JD70,000, (Around $100,000)
• Loan Maturity up to (72) months including a grace period.
• Maximum grace period of one year.
• The project has to be owned by the private sector and operating in Jordan.
• Loans under this program are decreasing loans without a prepaid interest.

Coverage:
• Guarantee Covers 70% (of the existing loan balance and interest rate of six months) for loans up to JD 70,000.
• The adoption of the principle of a partial guarantee for loans worth more that JD 70,000 (around $100,000) which does not fall under the terms of the industrial finance (EJADA).
Flexibility & adaptability

- JLGC own experience shows the need to introduce modifications in programs and procedures in order to meet changing requirements.
- Such changes became even more required following the International financial crisis which adversely affected domestic banking practices and intensified the reluctance of banks to extend credit.
- JLGC loan guarantee portfolio has accordingly been affected, going down by 8% in 2008 from 49 million Jordan Dinar against 45 million in 2007.
- JLGC has recently introduced the following changes in its programs & procedures to reduce banks reluctance and further encourage them to use the guarantee umbrella:
In addition to the Unified Standard Loan Guarantee Agreement signed between JLGC and individual banks, JLGC has signed recently special agreements with some banks to meet their specific needs and products.
JLG C started to delegate the guarantee decision to some banks in order to facilitate credit extension process to SMEs in accordance to specific conditions agreed upon between JLG C and banks. JLG C has recently started to provide loan portfolio coverage for some bank, instead of providing guarantees on undivided loans cases. JLG C has also introduced changes in the fees structure to take into account the size of activities guaranteed by participating banks and the risk involved.
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<tr>
<th></th>
<th>Loans</th>
<th>Export</th>
<th></th>
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<tbody>
<tr>
<td>Performance</td>
<td>$ (183 M) J.D</td>
<td>$ (500 M) J.D</td>
<td></td>
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<tr>
<td>Claims</td>
<td>3.335.894 J.D</td>
<td>320.000 J.D</td>
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<tr>
<td>Recovery</td>
<td>2.324.009 J.D</td>
<td>90.000 J.D</td>
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J.D = 1.4 $
## Fees (Pricing)

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<tr>
<td>Up To 1 M</td>
<td>1.5 %</td>
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<tr>
<td>From 1 To 2 M</td>
<td>1.25 %</td>
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<tr>
<td>More than 2 M</td>
<td>1 %</td>
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**EJADA Program:**
- **Case by Case**
- **Depend on:** Degree of the Risk