DRAFT GUIDELINES FOR LIVESTOCK FINANCING

Introduction

Agriculture is the most important sector of our economy that directly contributes 23% to the GDP, employs 42% of labour force, accounts for more than 60% of exports and provides raw material to most of the industrial and manufacturing base of the country. Livestock is the largest sub-sector of the agriculture accounting for 46.8 percent of value added of the sector and constitutes about 10.8 percent to the GDP. While the disbursements to the agriculture sector has witnessed an appreciable rise during the last few years as a result of sector friendly policies of SBP, the livestock sub-sector could not get its due share in the substantially enhanced flow of credit to the sector. During the fiscal year 2005, the Agriculture sector fetched credit of Rs. 108.7 billion, out of which the share of livestock was meagre Rs.6.8 billion or 6.2 % of the total disbursements.

In view of the significance of the sector in terms of contribution to GDP & employment and importance to serve as a vehicle to alleviate poverty rampant amongst the rural population where livestock is bred and maintained, the State Bank of Pakistan had established a Committee of Experts in August, 2005 to come up with some strategy / program for increasing share of institutional finance to this almost neglected sub-sector of agriculture albeit having huge potential for growth. The Committee has recently submitted its recommendations and SBP, on the basis of these recommendations, has framed guidelines to facilitate and encourage banks/FIs to build up their portfolio in the livestock sector. The guidelines cover all areas of the livestock financing business including products development and review, purposes and objectives of the loan, eligibility of borrowers, delivery channels, monitoring mechanism etc. The guidelines are suggestive and not mandatory in nature and give one of different ways to undertake livestock financing. Banks may adopt the guidelines in their present form or with adjustments suitable for their respective organization needs and market characteristics.

The Banks may consider establishing Livestock Research & Development Units at their Head offices to develop livestock financing products and their rollout in the field offices. The Unit could be a part of Agri/Rural Finance Division of the banks and be responsible for; a) Target market analysis, its characteristics, size, trends, growth potential etc, b) Development of products for livestock financing; c) Developing procedures for product marketing, delivery mechanism, monitoring mechanism, follow-up and recovery; d) Monitoring growth trends and quality of the portfolio and to develop close liaison with the field force to have feed back from the grass roots level; e) Review developments taking place in the livestock sector within the country as well as in other parts of the world.

Guidelines for Dairy and Meat Farm Financing

Dairy and Meat Farms constitute a significant proportion of the livestock sector. Pakistan is the fourth largest producer of milk in the world, however, only 2-3 % of the milk is processed. Similarly, the country has huge potential to develop meat farm and take its share in the attractive Halal meat market. Lack of access to adequate financial services has been among others a key impediment in growth and development of this sector. The guidelines are aimed at encouraging the banks to tap this sector that promises rich returns to the dairy growers, the banks and the economy as a whole. The easy and sustained access of Dairy and Meat Farms to affordable financial services would enable the Dairy and Meat growers to acquire modern, efficient livestock facilities, infrastructure and processing systems for milk and meat production thereby giving boost to livestock sector to produce large quantity of livestock products for domestic consumption as well as for export.

1. Types of Financing

The Dairy and Meat Farms need financing facilities both for long term investment for purchase of buffalos, cows, goats, dairy and meat farms equipments, construction of sheds etc. and also to finance their daily expenses/working capital requirements. The guidelines discuss three types of financing for the Dairy/Meat Farms viz. Working Capital, Term Finance and Composite Loans.

a) Working Capital Financing would inter alia cover following items:

- Purchase and plantation of animal fodder and feeds, feed grinders, tokas, feed mixing machines and feed/milk containers.
- Vaccinations, vitamins and other medications for animals including artificial insemination.
- Overhead expenses i.e. labour electricity /fuel etc.
- Utensils for animal feeding, calf feeders, bangles, Rope/Iron chains etc.
- Concentrate like cotton seed, cotton seed cake, other additional expenditure, distribution cost, transportation charges on farm milk processing, pasteurization, standardization.
- To finance receivables against deferred payment vouchers issued by milk processing units, sweets shops and meat processors/ traders/exporters having relationship with the bank and or enjoining good credit worthiness.

b) Term Financing would be for the purposes of:

- Purchase of mature milk yielding buffaloes/cows.
- Rreplacement of existing buffaloes/cows.
- Purchase of young buffaloes/cows/sheep & goats for rearing for meat production.
- Purchase of young animal/female heifers aged 3 to 4 years.
- Milk storage chilling tanks/ refrigeration plants and milk carrying containers.
- Refrigerated meat storages and refrigerated containers.
- Distribution vehicles such as motorcycles, pickups & refrigerated vans etc.
- Construction/procurement of permanent sheds, water tanks, water pump tube well and generators.
- Fencing and Enclosures.
- Establishment of slaughter houses (abattoirs)

c) Composite Loans Facility

- These loans are aimed at attracting small dairy and meat growers who constitute a bulk of livestock growers in the country and are generally hesitant to avail credit from banks.

- The composite loans would contain term finance as well as working capital to cater to the needs of small livestock holders for purchase of milch animals, young calf, goat, sheep for fattening etc. and 1-3 months feed / overhead expenses.
- The banks should design simple products for this market with the minimum possible documentation and repayments compatible with their cash flows from all sources.
- Such loans may be repayable in a period of upto 5 years in monthly instalments including a grace period of upto three months.

2. Eligibility

Individuals and corporates already undertaking livestock related activities or desirous to establish new dairy/meat farms may be extended the financing facilities provided the ACO/Branch Manager is satisfied with the capacity of the borrower/sponsors to manage and run the farm subject to the following conditions.

- The borrower should be a holder of computerized N.I.C.
- The borrower should not be a defaulter of any Bank/ Financial Institution. This condition may be relaxed in case the branch manager/ACO is satisfied with the creditworthiness of the borrower and that the earlier default was circumstantial and not wilful.
- ACO/ Manager/ RM are satisfied and comfortable with the farmer's and guarantor's (where applicable) identity, character, reputation & creditworthiness.
- The borrower must be living in the area for 5 years or more. However, this condition may be relaxed with the level of satisfaction of the Branch Manager/ACO to the background, character, capacity and repute of the borrower.
- Borrower Basic Fact Sheet containing detailed information about the borrower, as applicable in case of other agricultural loans, will be completed.
- It is advisable that the ACO has detailed understanding and information about the borrower as well as his capacity to effectively use and repay the loan and land, building and other capital assets he/she owns etc.

3. Fixation of loan limits and Repayment Terms

The limit amount may be assessed by the ACO/Branch Manager on the basis of financing request appraisal / feasibility report. Following parameters are recommended for this purpose:

a) ***Working Capital***

Purpose	Indicative, Financing Amount / Loan Basis Price	Mark- up Repayment	Maximum Period
Dairy & Meat Farms overhead including Purchase and plantation of animal fodder and feeds, labour, electricity, vaccination, medication & health care, artificial insemination etc. and low cost durables like utensils for animal feeding, calf feeders, feed grinders, tokas, feed mixing machines and feed/milk containers, bangles, Rope/Iron chains etc	**<u>Dairy Farm</u>** Rs.100-150 per cattle per day for maximum of 180 days working capital needs. **<u>Meat Farm</u>** Rs.100-150 per cow/buffalo and Rs.50 per goat / sheep per day for maximum 180 days working capital needs.	**<u>Dairy Farm</u>** Monthly based on the limit/amount utilized during the month. **<u>Meat Farm</u>** Quarterly based on the limit/amount utilized during the quarter.	**<u>Dairy Farm</u>** Limit to be extended for 1 year to be renewed / rolled over each year based on the following: • Loan account is regular; • No mark-up payment is overdue; • At least 6 out of the 12 months mark-up payments received within 10 days of the due date; • Payments equivalent to at least 15% of the maximum amount utilized have been received during the year. **<u>Meat Farm</u>** Limit to be extended for 1 year to be renewed/rolled over each year based on the following: • Loan account is regular; • No mark-up payment is overdue; • At least 2 out of the 4 quarters mark-up payments received within 10 days of the due date; • Payments equivalent to at least 15% of the maximum amount utilized have been received during the year.
To finance receivable against Deferred Bills.	80% to 90% of the Deferred Bills (in order to cover both principal and accrued mark- up)	Through realization of the Deferred Bills	Each Deferred Bills amount to be cleared within 90 days of financing/discounting.

b) ***Term Financing***

i. Dairy Farm

Purpose	**Indicative Financing Amount/Loan Basis Price**	**Repayment**	**Maximum Period**
Purchase of mature milk yielding buffalos/ cows.	Maximum Rs.50, 000/ per buffalo and Rs.40,000/= per cow or up to 80% of actual cost whichever is lower.	Monthly	Up to 5 years including grace period up to 3 months.
Purchase of young animals for rearing for dairy purposes,	Maximum Rs.10,000/- per buffalo and Rs.6,000/- per cow or 80% of actual cost whichever is lower.	Monthly	Up to 5 years including grace period up to 3 months.
Milk storage chilling tanks/ plants and milk carrying containers (To be allowed for Dairy farms having more than 20 animals)	Maximum 80% of the purchase price/ cost (average of at least 3 quotations)	Monthly	Up to 5 years including grace period up to 3 months.
Distribution vehicles (motorcycles, pickups refrigerated vans) (To be allowed for Dairy farms having more than 20 animals)	Maximum 80% of the purchase price/ cost (average of at least 3 quotations)	Monthly	Up to 5 years including grace period up to 3 months.
Construction / procurement of permanent sheds, water tanks. Purchase of utensils for animal, water pump and generator.	Cost should be assessed by banks evaluator. Maximum 80% of the purchase price/ cost (average of at least 3 quotations)	Monthly	Up to 5 years including grace period up to 3 months.

ii. Meat Farm

Purpose	**Indicative Financing Amount / Loan Basis Price**	**Repayment**	**Maximum Period**
Purchase of young buffaloes/cows / sheep and goats for rearing for Meat purposes.	Maximum Rs.10,000/- per buffalo, Rs.6,000/- per cow and Rs.3,000/- per sheep/goat or 80% of actual cost whichever is lower.	Quarterly/Half yearly	Up to 5 years including grace period up to 3 months.
Refrigerated Meat storage and refrigerated containers	Maximum 80% of the purchase price/ cost (average of at least 3 quotations)	Quarterly/Half yearly	Up to 5 years including grace period up to 3 months.

Distribution vehicles (pickups & refrigerated vans)	Maximum 80% of the purchase price/ cost (average of at least 3 quotations)	Quarterly/Half yearly	Up to 5 years including grace period up to 3 months.
Construction / procurement of permanent sheds, water tanks. Purchase of utensils for animal, water pump and generator.	Cost estimation should be assessed by banks evaluator. Maximum 80% of the purchase price/ cost (average of at least 3 quotations)	Quarterly/Half yearly	Up to 5 years including grace period up to 3 months.

iii. Composite loans for Small Dairy & Meat farms

Purchase of cattle and other items term eligible for term finance and working capital needs for 1-3 months.	The finance limits to be determined based on indicative prices/limits discussed above for both term finance and working capital.	Monthly with 3-month grace period.	Up to 5 years including grace period up to 3 months.

4. Markup

- Banks are free to determine mark up rate based on their cost structure and risk profile of the borrower and livestock sector.
- There will be no penalty on early repayments / adjustment

5. Security

- ***For loans upto Rs.5 Lacs.***

  Primary security

  - Personal Surety.

  Secondary security (at the discretion of the Bank)

  - Hypothecation of cattle/buffaloes/ cows/goats/sheep, identified by putting bangle/ring, having bank ID on one front leg/ neck of the animal, or any other alternative ID chosen by the bank.

- ***For loans exceeding Rs.5 Lacs.***

  - Hypothecation of animals, as in case of loans upto Rs.5 Lacs.
  - Secondary Collateral (at the discretion of the banks) and Indicative Margin Requirement there against are as follows:

Collateral	Margin Requirement
Mortgage of Agriculture land* & Rural, urban or commercial property.	50 % of market value
Pledge of SSC/DSC etc. Lien on bank deposit.	0% of encashment value, covering principal and 6 months mark up.
Pledge of gold and gold ornaments.	25% of valuation by the bank's approved gold smith. (Mark to market annually.)
Individual / Group / NGOs Guarantee.	1. Should provide coverage to Principal alongwith one year mark-up. 2. Maximum per person exposure as mentioned in PRs for Agriculture regarding personal guarantee.

*Market values of land would be assessed by the ACO/Branch Manager by visiting the site and collecting necessary information about the land. However, for the guidance of the lending banks indicative per acre upper limits for Barani, tube-well irrigated and canal irrigated lands are Rs.50,000/-, Rs.100,000/- Rs.200,000/-respectively.

- The hypothecated animals should be comprehensively ensured from reputed insurance company or group of companies against death, theft and burglary etc. It is advisable that banks should sensitize and educate their borrowers about the critical importance of having an insurance cover and should make insurance as an integral part of their respective livestock financing products.

6. Channels of Financing

- Direct Financing to Dairy/Meat Farms.
- Indirect Financing to Dairy/Meat Farms through Milk/Meat Processing Units etc.
- Financing against Deferred Bills issued by reputed Milk/Meat Processing Unit.
- Discounting of Deferred Bills.

Further details about the loan delivery mechanism and marketing of loans may be seen at Annexure -1 to the guidelines.

7. Documentation

Following documents / formalities must be completed:

- Bank account in the name of intending borrower before applying for the finance.
- Standard Application Form (SBP format) in Urdu along with borrower and his/her father / husband name in English (for feeding in computer with correct spelling) duly completed, should be obtained. Signatures/Thumb impression of the Applicant, Guarantor and Witnesses (where required) and verified by the Branch Manager.
- In case of Tenants / Haris a certified copy of Khasra Girdawari, Fard Jamabandi or Form VII & VII A (for landowners of Sind Province)

or

- Bank charge may be created on the agriculture land through Pass Book System by the Revenue Authorities and a charge creation certificate schedule - II is to be obtained

or

- Registered or Equitable Mortgage of rural/urban property **or** earmarking of Bank's Deposits, **or** pledge of DSC/SSC/Regular income certificates/other financial instruments **or** pledge of gold, silver and gold and silver ornaments.
- Letter of agreement-cum-guarantee (IB-7 *revised*) from the borrower.
- Appraisal Report on the applicant and Credit Report of the guarantors must be prepared before finance is sanctioned.
- SBP Credit Information Report (CIB) should be obtained.
- For loans against the continuing guarantee and charge on fixed / current assets of the processing units. The processing units will provide a list of their bonafide milk providers along with their computerized NIC numbers and addresses. Finance would be disbursed in the account of milk processing unit for onward disbursement to their milk providers. The processing unit will be responsible for repayment of loan as per terms and conditions agreed between the bank and the processing unit.
- Completion of documentation shall be the responsibility of ACOs /Managers /RMs.

8. Conditions/Covenants

- Submission of Financial/Income & Expenses Statements should be encouraged. It should be mandatory for Dairy/Meat Farms having 50 or more cows/buffaloes and 100 goats/sheep. If specified in Approval of Finance, to be obtained accordingly.
- Submission of periodic inventory record at least on quarterly basis.
- For Financing more than 50 cows / buffaloes or 100 sheep/goats the following should also be observed:-
  - Submission of product marketing plan for next six month on bi-annual basis.
  - Feed procurement source, quantity & pricing plan on biannual basis.
  - Vaccination through Doctor authorized by Branch/ RM.

9. Loan Monitoring System

Effective loan monitoring and tracking system are critically important for ensuring quality of the agricultural loan portfolios. The banks may develop sound and reliable loan monitoring and tracking system to venture into livestock sector with confidence. Some details about the loan monitoring and tracking system have been given in Annexure-1

10. Recovery of Loans

First recourse for the bank to recover its loans is the borrower and his/her cash flows. The effective monitoring system and follow-up and frequent interaction with the borrowers is critical for ensuring recovery of agricultural loans. The traditional correspondence and letter/notice based recovery mechanism will not be successful in agricultural loans. Considering the low tickets and large volume nature of agricultural and rural credit it would not be cost effective to send payment request letters particularly to the small clients. The following recovery proceeding, however, should be initiated against the delinquent borrowers who don't make payments through normal follow-up and persuasion methods:

- Persuading borrowers / guarantors through personal contacts.
- Issuance of legal notices.
- Persuasion through Recovery Tehsildar / Mukhtiarkar after declaration of loans as Arrears of Land Revenue in accordance with Section 4(7) of Loans for Agriculture Purposes Act 1973 by the Collector / Asstt. Collector / Deputy Commissioner in case of financing against passbook.
- Filing recovery suits in Banking Tribunals/High Courts.
- Any other legal remedies available to the bank.

11. Special Precautions

- At least bi-annual inspection by bank's trained officer or an independent veterinary doctor from an institution recognized by H.E.C. Necessary action should immediately be taken in the light of the inspection report.
- Vaccination against contagious diseases.
- Periodic proper diagnosis and care of sick animals.
- Encouraging artificial insemination of cows and buffalos from reliable sources.

12. Non Performing Loans (NPLs)

- Classification as per procedure of SBP Prudential Regulations for Agricultural financing.

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Annexure-1

Guidelines for Livestock Financing

Delivery Channels/Marketing of Loans

a) Direct financing to livestock owners/farmers

- The traditional commercial banking approach of waiting the clients to visit branches to avail financial services normally doesn't work for agricultural loans. The banks therefore will have to devise innovative and cost effective mechanism to reach to the clients and market and sell their products.
- The branch / area Managers should develop a comprehensive data base about the area/region the branch is supposed to serve consisting of the numbers of districts towns, union councils, villages in the area and their demographic data; the total cultivatable area, major crops, fruits, vegetables, the livestock statistics, no. of dairy farms, meat farms, cattle breeding farms; average number of cattle in each households; the level of presence of other Financial Institutions (FIs) etc.
- The ACOs/MCOs should be assigned the union councils and villages to be covered during a specified period along with the portfolio build-up targets.
- The Regional Managers/ACOs should arrange meetings with the villagers/farmers, livestock growers to introduce the products and services they are offering for the farm, non-farm and livestock sectors.
- The meetings should be arranged in consultation and collaboration with the active and influential persons of the village/area like Mosque Imams and Chaudrays etc. so that maximum number of villagers could be informed about the products. The meeting should be focused, standardized and time bound.
- After the introductory meeting the ACO should follow-up with the interested farmers/dairy growers for extending farm and non-farm products.
- The branch in rural areas or in small towns adjacent to rural areas should be designated as Agricultural and Rural Finance Branches and given specific business targets for agricultural credit and encouraged to become more and more mobile to market the bank's agricultural products.

b) Indirect lending/ financing

- Indirect lending may be made through milk processing units, sweet shops, biscuit manufacturers, ice cream parlours etc.
- The banks may either provide loans to the milk processors for onward lending to livestock growers on guarantee of the processing units etc or directly to the growers against the Deferred Bills issued by the processing unit.
- The wholesale funds to the processing units will however, be properly secured against charge on the assets of the processing unit, mortgage of rural/urban properties etc.

- For financing against Deferred Bills or discounting of Deferred Bills, the issuer of Deferred Bills should have relationship with the bank with automatic liquidation mechanism.
- The working capital facilities may also be extended against the Deferred Bills issued by reputed corporates not necessarily having any formal relationship with the bank. For the purpose however, bank should ensure that the issuer is a creditworthy party enjoying an impeccable track record of timely repayments and that the bank has some mechanism for verifying authenticity of the Deferred Bills.

The bank should also develop. Banks may also extend wholesale funds to reputed NGOs/MFIs for onward disbursement to livestock growers. The banks should develop criteria for selection of NGOs for extending the whole sale funds.

Monitoring

Weak and traditional monitoring system of agricultural loans has also been one of the important reasons for low growth in agricultural and rural finance sector. The exceptionally good recovery rate of reputed Micro Finance Institutions (MFIs) across the world is attributable among others to effective loan monitoring systems developed and adopted by the MFIs. It is therefore advisable for banks to:

- Develop sound and reliable loan monitoring systems to venture into livestock sector with confidence;
- Impart necessary training to their ACOs in loan marketing, borrower appraisal, background checking, and cash flow analysis, monitoring and follow-up;
- Develop MIS capacity to generate timely reports for effective monitoring and follow-up by the ACOs. The MIS should provide an effective loan tracking mechanism and generate loan officer- wise and district/town/union council wise disbursements, recoveries, outstanding, delinquencies reports etc. to facilitate the ACO/Branch Manager in loan tracking, monitoring and recoveries;
- Develop mechanism for carrying out regular follow-up and monitoring of the loans;
- Monthly visit of ACO to each borrower is advisable;
- The Branch Managers / Relationship Managers may also personally visit 5%-10 % of the clients on random basis in each quarter based on the reports generated by MIS.

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