

‘Gem and Jewelry’



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Address
Infrastructure, Housing & SME Finance Department,
State Bank of Pakistan
I.I. Chundrigar Road,
Karachi
Ph: 021-32455501, 021-111 -727- 111
FAX: 021-99221139

Acknowledgement

This segment booklet has been developed by M/s Corporate Partners (CDP) who was commissioned by State Bank of Pakistan (SBP) to conduct the market research.

SBP's Infrastructure, Housing and SME Finance Department provided critical facilitation and oversight for this initiative. State Bank of Pakistan is the Central Bank of the country. Like a Central Bank in any developing country, State Bank of Pakistan performs both the traditional and developmental functions to achieve macro-economic goals. This role covers not only the development of important components of monetary and capital markets but also to assist the process of economic growth and promote the fuller utilization of the country's resources. The role of DFID, UK is also acknowledged here as the cost of the research study was funded by this organization under the Financial Inclusion Program.

This report contains market research and proposed banking products, based on primary research survey results and secondary sources, carried out for SME segment 'Gem and Jewelry' by Corporate Development Partners (CDP).

The purpose of this research report is to provide segment specific credible information for the commercial banks to facilitate them in designing and delivery of banking services to small and medium enterprises (SMEs) in a responsible, profitable and sustainable manner.

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1 Guidelines for using this Research Report

The '*Gem and Jewelry*' Segment Research Report provides indicative business and financial characteristics based on the information derived from a sample of business owners via primary research survey. It can be used by Banks/DFIs as a starting point for development of program based lending products for tapping the underutilized potential for providing financing products to '*Gem and Jewelry*' business owners.

The '*Gem and Jewelry*' Industry overview is developed by using information obtained from secondary and tertiary sources, including industry associations and data available in public domain.

1.1 Market Assessment

This section contains analysis based on primary findings of survey exercise conducted in main cities of Pakistan, majorly Karachi, Peshawar and Rawalpindi among others; the information can form the basis of identifying the characteristics of a typical business entity in the segment.

1.2 Product Suite

Proposed banking product suite provides a number of potential core banking products templates that can be used by Banks/DFIs to design appropriate banking products for gaining access to the particular segment. However, it is highly recommended that product development undergoes the usual general practice and protocols employed by the bank. It is also recommended that the product development and the business line team work together to conduct a quick market research of a small sample in order to validate the results of this study.

1.3 Marketing and Distribution

Marketing and Distribution considerations are indicative and have been based on the assumption that banks will employ their individual marketing and distribution strategy for product development. However, information presented can be utilized by banks for developing certain hypothesis to be validated for developing their marketing and delivery strategies.

2 Introduction & Objectives

According to the latest data cited in SMEDA and Economic Survey Reports 2010-2011, Small and Medium Enterprises (SMEs) account for approximately 40% to GDP contribution of Pakistan and play a major role in spurring economic activity with a contribution amounting to 80% of non-agriculture GDP of Pakistan. Many businesses in this '*Gem and Jewelry*' segment have used banks for business needs but with very few using it as a source of business fund. This is mainly due to the following impediments:

- A different risk profile
- Lack of substantial collateral
- Conservative approach adopted by financial institutions
- Lack of awareness and willingness of banks

SMEs present immense business opportunities for financial institutions from the perspective of increasing book size while generating strong risk adjusted returns, however there is an imminent need to understand the dynamics of this segment in order to enable financial institutions to structure products that meet overall risk management guidelines and facilitate the growth of this SME segment.

In this context, State Bank of Pakistan (SBP) has mandated Corporate Development Partners to conduct a secondary research and a primary survey of ten major SME subsectors of Pakistan to determine banking and financial needs of the sector.

This research report contains findings pertaining to the segment of "*Gem and Jewelry*" which includes gem cutting and polishing units as well as jewelry manufacturing units.

Manufacturing sector in Pakistan has been the major contributor towards promoting economic growth, however, lack of research and development and inadequate investments has restrained this sector to reach its growth to the fullest potential. Service sector in Pakistan has emerged as a major contributor towards promoting economic growth and recently went through major transformation with share of service sector increasing to 58.1% of the GDP, while the mining sector estimated to grow at 4.4% in the year 2013-14 (Economic Survey 2013-14). With more focus being placed on the service sectors, these sectors have the capability to reach growth to the fullest potential.

The '*Gem and Jewelry*' Sector consists of:

- *Precious raw gem and gemstones*
- *Jewelry manufacturing*

The processing units of gemstones are mostly located in the mountainous regions of Pakistan where gems in raw form are extracted. Khyber Pakhtunkhwa province has the largest deposits of gems. The jewelry sector consists of jewelry manufacturing units which are located most in the

urban cities of the country where the jewelry retail shops are located. Raw gems and gold is transported from the Gilgit-Baltistan, KPK and AJK to the cities where they are used in the jewelry making process.

The sector of precious raw gem and gemstones is highly unorganized and lacks severely in updated technology for cutting and polishing of gems. This sector has great potential in growth and export (USD 1.18 billion in 2013 - PGJDC) and therefore requires investment in polishing and cutting of gems and state of the art equipment for jewelry designing. This will help the sector in generating revenue as per its true potential/capacity.

2.1 Limitations of the Study

- The sample may not be geographically exhaustive.
- The sampling plan may not suit the requirements of every bank.
- Some of the recommendations are not backed by quantitative primary research but are based on knowledge of the market and best practices.
- Some of the questions in the questionnaire, especially in the financial information section were considered too personal by many business owners; therefore, many of them refused to answer. Hence, the responses in this regard may be evasive and cannot be verified with respect to their accuracy.

2.2 Sampling Plan

The primary research exercise conducted for identifying the financial needs of the SME segment was based on the following sampling methodology.

Table A: Sampling Plan

Particulars	Criteria	Rationale
Size	<ul style="list-style-type: none"> 1,000 detailed one-on-one interviews for 10 sub-sectors 100 SMEs surveyed within each sub sector. 	<ul style="list-style-type: none"> Sample size is sufficient enough to gather relevant qualitative and quantitative information on each sub sector Increase in the sample size will only add marginal value to the overall information collected from the survey exercise <p>Change of Definition of SME by SBP</p> <ul style="list-style-type: none"> Small enterprises are defined as those businesses that have employees up to 20 and annual turnover up to PKR 75 million Medium enterprises are businesses with more than 20 employees and turnover above PKR 75 million and up to PKR 400 million for the purpose of classification and segmentation by banks For the purpose of this research, the small portion of medium entities that we have reviewed include entities that have revenue up to PKR 150 million (i.e. two times the sales of Small Enterprises)

Particulars	Criteria	Rationale
Status	<ul style="list-style-type: none"> At least 60% will be informal businesses At least 20% will be formal businesses 	<ul style="list-style-type: none"> Informal businesses would be entities that do not have formal accounting and book keeping system. They do not get their accounts properly audited and are normally not registered under an official trade/regulatory body. A wide majority of businesses operating in Pakistan are informal businesses in terms of their quality of record keeping and accounting information, in the absence of which banks do not offer them any credit based products. A study of informal businesses enables us to gauge the reasons of these proprietors to remain within the informal segment and still compete in the market with formal business enterprises within the same industry segment. Moreover as per revised SME Prudential Regulations, Small businesses are allowed financing up to PKR 15 million without the audited financials. This regulatory change will enable SMEs to qualify for a structured lending product by maintaining the basic system of book keeping and accounting. Formal businesses are those entities that are relatively larger in size and have a proper book keeping system. These are also registered businesses that are operating either under an association of businesses or under a formal regulatory license, with a fair amount of transparency in their accounting and book keeping systems Including the above businesses give us a fair representation of entities that are eligible for all financial services being offered by banks and their extent of using banks as their main financiers and other service providers or only for holding their business operating accounts Formal businesses have more structured requirements than those who use banks only for products such as fund transfers

Particulars	Criteria	Rationale
Turnover	<ul style="list-style-type: none"> At least 50% with turnover less than PKR 75 million At least 20% with turnover more than PKR 75 million 	<ul style="list-style-type: none"> The corresponding sample mix has been adopted to ensure majority coverage of small businesses in the overall sample size since these would be the primary candidates for programme lending products However, for the purpose of understanding the financial needs of medium sized entities that are close to the threshold point of small and medium, we have covered a minor portion to understand their requirement for structured loan products as well as other financial services generally required by businesses that are relatively mature and larger sized than small enterprises
Employees	<ul style="list-style-type: none"> 60% will have less than 20 employees 40% will have more than 20 employees 	<ul style="list-style-type: none"> SMEs that are not in the manufacturing segment are relatively understaffed owing to the small size of their business and ease of management Moreover, businesses that have more than 20 employees will now be classified as medium sized hence we have covered a substantial portion of such entities as well

Particulars	Criteria	Rationale
Banking history	<ul style="list-style-type: none"> At least 70% with banking history At least 10% with no banking history 	<ul style="list-style-type: none"> As per SBP prudential regulations any business operated by an individual as proprietor, but meets the classification criteria of the regulations will be termed under SME On account of above a majority of sample in the market are operating their businesses through a bank account (either in the name of the proprietor or in the name of the business) Most of the financial needs and preferences that are objectives of this assignment, have been obtained from the above sample who are using a bank for their businesses operating needs However, a very small portion of the totally unbanked SMEs in the sub-sector is also covered during our survey to understand their reasons for not availing the banking services and fulfilling their needs for financial services through other, more expensive, informal channels

3 Economic Overview

Pakistan's economy has shown resilience despite challenges which include domestic factors such as political instability during the last few years, security situation and international financial crisis, in addition to an unprecedented rise in food and energy prices. As per the Economic Survey of Pakistan (2013-14), after a period of slow growth due to floods and law and order crises, the economy showed a significant growth in 2013-14 on the back of immense recovery from the industrial sector along with moderate growth in agriculture and service sectors. With industrial sector expanding by 5.84% when compared to last year figure of 1.37%, while the economy grew by 4.14% in FY-2014.

Table B: Economic Considerations

Positives	<ul style="list-style-type: none">▪ Heavily populated, (over 180 million people) translating into strong future potential for improvement in work force as well as purchasing power, leading to growth in consumer related segments.▪ Despite many challenges faced by the country, Pakistan has performed better than many developing countries with the GDP growth rate of 4.14% in FY 2014 which is highest in the last three years when compared with GDP growth in FY 2013 and FY 2012 of 3.7% and 3.84% respectively.▪ Rising rates of urbanization – with the UN forecasting the proportion of city dwellers climbing from 34.9% of the population in 2005 to more than 50% by 2035 – should continue to serve as a key driver of economic growth.▪ The industrial sector showed a huge growth of 5.84% compared to previous year of 1.37% which has been a huge boost to the economy as it contributes to 20% of the GDP. It is also a major source of tax revenue.▪ Investment activities are continuing to take place, backed by the fact that public investment has recorded a remarkable growth of 17.12% while last year it had a negative growth of 0.35%.▪ Foreign Direct Investment (FDI) has also shown a remarkable increase from USD 1,277 last year to USD 2,979 in the period July – April 2013-14, an increase by 133%. Major portion of FDI was for oil & gas exploration, electricity & power, financial business and chemicals.▪ Positive trend of remittance over the last 10 years has greatly supported
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the country's balance of payment position.

Challenges

- National saving is showing a decline, with 12.9% of GDP in FY14 while in FY13 it was reported 13.5% of the GDP. Covering the saving-investment gap remains to be a challenge.
- The FY 2013-14 has shown slight improvement in fiscal deficit which reduced by 3.2% compared to previous year. Structural weakness in tax system however still prevails with low tax to GDP ratio while the expenditures continue to exceed the revenues.
- Balance of payments has shown a surplus of USD 1,938 million compared to last year deficit of USD 2,090 million in FY 2013-14. However despite that, the current account balance further showed a deficit of USD 2,162 million in July-April 2013-14 compared to last year in the same period.

4 'Gem and Jewelry' Industry Overview

Table C: Summary of Industry Overview

Factors	Comments
Demand	Pakistan has great potential in increasing its exports of jewelry and more so in gemstones, which are available in abundance. The gemstones however are exported in raw form due to lack of sophisticated technology for gem lapidary. Jewelry manufacturing is mostly available in traditional designs which are valuable in Pakistan but do not match the international demand.
Supply	Pakistan has one of the biggest natural reserves of gemstones and gold with vast areas still undiscovered. Unfortunately due to lack of sophisticated technology, gems are not extracted with proper technique, leading to wastage as well as compromise in terms of quality.
Key players	Pakistan Gems and Jewelry Development Company, Shabeer gems minerals collection, Chotani Jewelers, H. Jamal & Sons Jewelers etc.
Trade Bodies	<ul style="list-style-type: none"> • All Pakistan Gems Merchants and Jewelers Association (APGMJA) • All Pakistan Commercial Exporters Association of Rough & Unpolished Precious and Semi-Precious Stones (APCEA)
Regulatory Body	Ministry of Industries
Recent Development	This sector has been realized to be one of the major potential revenue generating sectors. Steps have been taken by government to support it. Many training institutes are being set up to raise the skilled workforce as well as create awareness for international demands and quality standards.
Future prospects	With more government support and introduction of state of the art technology in both mining and manufacturing segment, this sector has huge potential to be one of the top players in the international market.

4.1 Precious raw gem and gemstones

4.1.1 Demand

Pakistan is a country fortunate to have unmatched quality of Ruby, Emerald, topaz, aqua marine, fluorite, lapis-lazuli which are mined from the valleys of Gilgit, Hunza, Swat, Azad Kashmir and Chitral. Due to non-availability of gem cutting and polishing facilities, gems are exported in a raw form, which is insignificant in value as compared to their real worth. Major gem export markets include Thailand and Sri Lanka, along with West Europe, USA and East Asia. Besides higher priced and more in demand gemstones like Emerald, Pink Topaz and Ruby, Pakistan also has one of the largest deposits of other gemstone varieties.



Many units involved in the cutting and polishing of gems use outdated and simple technology, the end product does not hold much value by the traders and exporters. Therefore almost all these gems are exported in raw form, from which many are smuggled in the neighboring countries like China and Afghanistan.

Mainly due to lack of proper infrastructure, poor mining knowledge and lack of technology and technical know-how, this industry has not been able to establish itself amongst the top 5 markets internationally.

4.1.2 Supply

Pakistan is abundant in its natural reserves of precious stones. Peshawar is called a 'gems city' as gem-buyers crowd this city in search of precious stones. Gems include precious or semi-precious categories like rough, uncut or cut and polished or unpolished stones, pearls, diamonds and corals like emeralds, topaz, lapis, peridot, sapphire, kunzite, ruby, aquamarine etc.



Pakistan is also known to have fifth largest gold mines¹. There are still many untapped reserves, which still need to be developed. If gems sector is fully developed, it can generate immense revenue and contribute hugely to the country's economy. This sector has big potential but the current state is very poor and a large quantity of the precious and semi-precious stones are exported in raw form due to unavailability of gem cutting and polishing machinery. These raw

¹ <http://www.thenews.com.pk/TodaysPrintDetail/2011>

forms of gems generate low profit, which is negligible compared to their actual worth. Therefore, Pakistan has billions of dollars foreign exchange earning capacity, if it focuses on exporting value-added products of gems and jewelry instead of selling it abroad in raw form. However, sadly many countries are taking advantage like China, Afghanistan, USA, Belgium, UK, India etc., and import gems from Pakistan in raw form, preferring to use their own lapidary techniques.

4.2 Jewelry manufacturing

4.2.1 Demand

Gold jewelry has not only been perceived as a symbol of status and wealth but also holds a great traditional value, which is attached to every family in the subcontinent. Many people perceive it to be as a source of investment security and savings as well.



Demand for gold jewelry rises to its peak during wedding seasons, which is mostly in winter and spring. Highest demand is for 22-karat gold by Pakistan and India, while for 14-18 karat gold, the key market exists in West and Far East. With the overall increase in working population and a rise in purchasing power, many are using gold as a medium of savings for future. More recent trends indicate their preference is also shifting towards 18-karat gold.

The biggest importer of gold jewelry from Pakistan is Dubai followed by USA and UK. Despite high demand, the tools and technology used are not very updated. This has resulted in the jewelry industry to lose its export share compared to other international players with India being the biggest competitor.

Gold jewelry export can increase at least ten fold if designs are also focused towards the international market which is more light weight and separate from the heavy traditional designs. Also a high demand is placed on 18, 14 and 8 karat gold while in Pakistan mostly jewelry is based on 22 karat gold.

4.2.2 Supply

Gold jewelry manufacturing is labor intensive and requires high level of skill, which is usually passed on from generations to generations. Different gold jewelry manufacturing units have different specialization in specific processes and skill. Therefore these units are clustered as an independent unit, each specializing in their own process and sending their finished goods for further processing to relevant units. Each unit is dependent on each other for their skills and completion of the final product. Highly skilled manpower is



however mostly concentrated in major cities like Karachi and Lahore. This segment is still quite unorganized and therefore proper data of the number of units established is not available.

The machinery used in this segment is locally made and is stated to be at par with Italian machines. Due to this fact the machines are not very costly and so less investment is required. However major challenge that jewelry making segment has to endure is to stay updated in jewelry designs that are demanded in the international market.

The jewelry manufacturing can be in-housed or outsourced. The establishment of in-house manufacturing is opted by jewelry manufacturers to ensure their designs are not copied elsewhere, giving them an edge in competition. It is however not feasible for small scale jewelry shops to have an in-house jewelry manufacturing unit because of the cost associated with it.

4.3 Key Players

The major key players of '*Gem and Jewelry*' Sector are Pakistan Gems and Jewelry Development Company, Shabeer Gems & Minerals collection, Chotani Jewelers, H. Jamal & Sons Jewelers, etc.

4.4 Trade Bodies

- All Pakistan Gems Merchants and Jewelers Association (APGMJA) has been working as a facilitator to various tasks related to '*Gem and Jewelry*' sector as well as handling the emerging problems in this industry. The main aim has been to regulate the market and enhance the quality of the product, to be able to compete in the international market.
- All Pakistan Commercial Exporters Association of Rough & Unpolished Precious and Semi-Precious Stones (APCEA) has been established to aid in export of rough and unpolished precious and semi-precious stones as well as to frame rules and regulations governing trade in this sector.

4.5 Recent Developments

'*Gem and Jewelry*' sector is being considered by the government as an important and active industry which has huge revenue earning potential and of becoming one of the leading exporters in the international market.

Also training institutes such as Gems and Jewelry Training and Manufacturing Centre have been set up which are now offering postgraduate diplomas with prime focus on jewelry designing and manufacturing.

4.6 Future Developments

With more government support and introduction of state of the art technology in both mining and manufacturing segment, this sector has huge potential to be one of the top players in the international market.

PGJDC is participating in different international Jewelry Exhibitions where Pakistani companies are not only getting export orders but also learning about the latest trends in jewelry designs as well as the requirements of international markets.

4.7 Gemstone Cutting and Polishing

Following is the gemstone cutting and polishing procedure:

Sawing: Gemstones are cut and shaped by a thin circular blade with water or oil used to wash away the debris and prevent the blade and stone from overheating. Different sizes of saw blades are used for different depth in cutting.

Grinding: Gems are shaped in a desired rough form by machine with diamond impregnated wheels.

Sanding: Deep scratches that are left behind by grinding process are removed using finer abrasives and also allows for finer shaping of the gem.

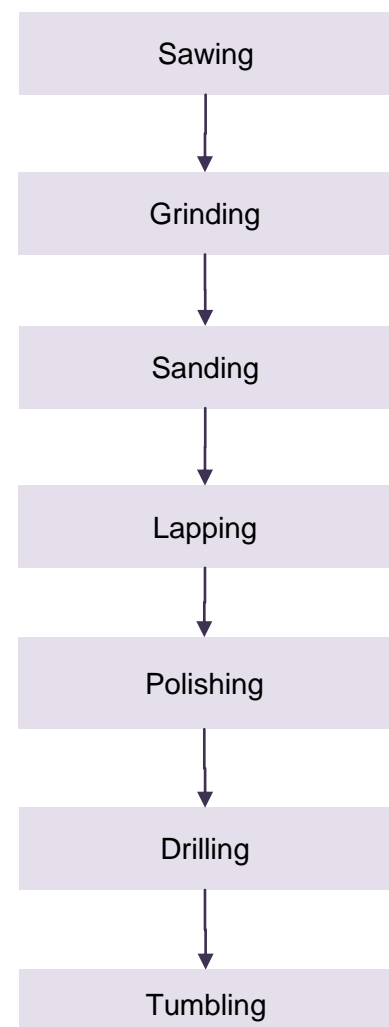
Lapping: A rotating and flat disk is used to give flat shape to gems.

Polishing: The gems, once shaped, are then polished, giving it a shining surface.

Drilling: If a hole is required to be made through the gem to create beads, those gems are drilled through using small rotating rod of diamond tip.

Tumbling: The remaining large rough stones are then turned in a barrel at a slow speed with water and abrasives for days resulting in fine and smoother stones of attractive shapes.

Figure 4.7-a: Gemstone Cutting and Polishing Process



4.8 Jewelry Manufacturing Process

Initially an order is placed after which following process takes place (**Figure 4.8-a**):

Jewelry designing: A process of blue print designing is carried out, which is copied from catalogues provided by the customers or designed by the jeweler himself.

Molding: The designed jewelry is then turned into a plastic mold, which sets the base for total jewelry making process.

Casting: This is a complex process, which involves steel containers in which wax molds are placed. The metal of choice (gold, silver, etc) is poured into the mold and allowed to cool. The mold is then removed revealing the jewel casting

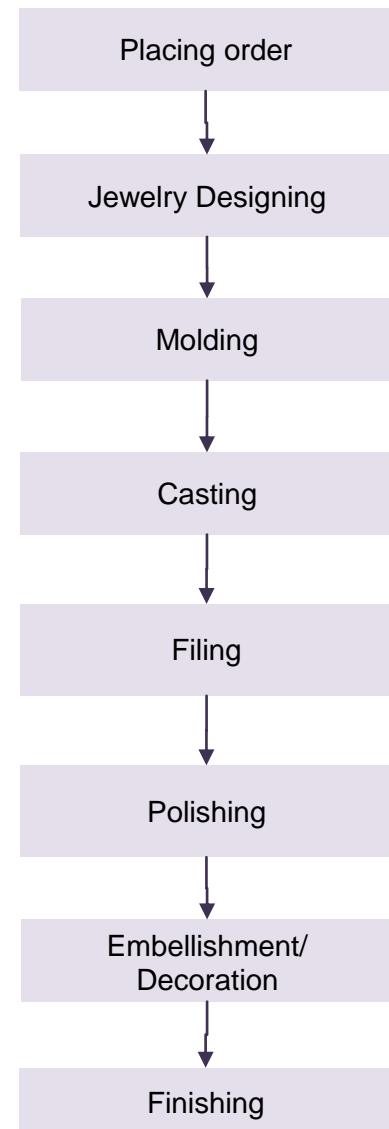
Filing: Filing is used to remove excess metal, even out surface, smooth or shaped, as required.

Polishing: Every part of the jewelry is polished, also ensuring no part of mold remains.

Embellishment/Decoration: The required decorative stones and gems are cut and weighed with preciseness and assorted for final setting in jewelry.

Finishing: The casting in this process is given attention for smooth and soft finish in order to meet high standards.

Figure 4.8-a: Jewelry Manufacturing Process



4.9 Success and Survival of the Businesses in this Sector

From the survey interviews (*Figure 4.9-a*), 79% of the business owners felt that good relations with the suppliers and 34% of the business owners felt that timely delivery of the finished goods was the major success factor for the businesses in this sector.

In order to survive as an SME (*Figure 4.9-b*), 89% of the business owners believe that experience was the most essential element followed by education by 70% of the business owners. 14% also felt that due to favorable government policies their business set up has managed to earn profit throughout these years, while 8% of the business owners further added that due to strong supplier customer relations their SME businesses managed to survive.

Figure 4.9-a: Indicators of Business Success

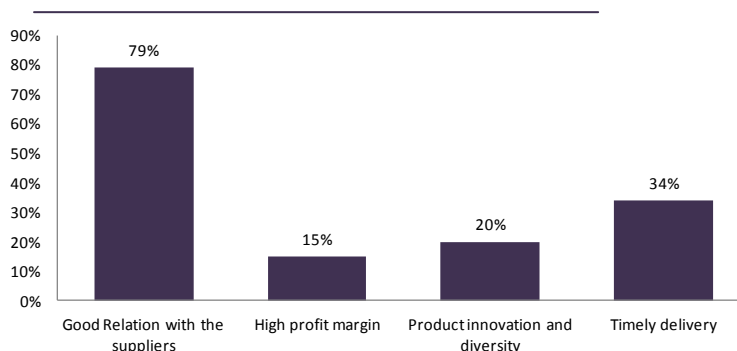
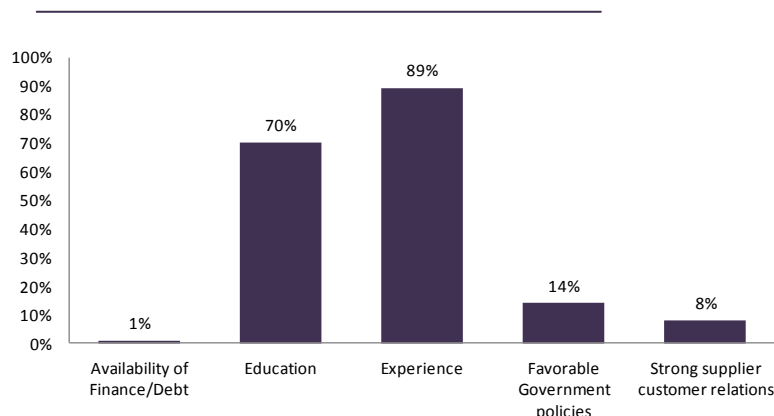


Figure 4.9-b: Key means of survival as an SME



Source: Survey Findings

5 Market Assessment

5.1 Market & Demographic Profile

Most businesses in the SME sectors are family owned with members of one family serving different functions of business. Underlying issues inherent to the segment include:

- 1) Limited funding sources and capital investment in unorganized sector
- 2) Lack of innovation and research within the sector
- 3) Lack of access to complete retail data
- 4) Unorganized infrastructure
- 5) Lack of awareness and willingness of banks
- 6) Use of outdated technology by the gem sector

The '*Gem and Jewelry*' Sector may be considered as unorganized in terms of structure if we assess the Gem industry. However, Jewelry manufacturing and retail shops are considered to be comparatively more organized but only in Karachi and Lahore clusters. Gems sector is concentrated in Gilgit-Baltistan and KPK, with highest number of establishments present in Peshawar, where reserves are present in abundance. Jewelry manufacturing and retail sector has many clusters in Karachi and Lahore where it is in close proximity to the target market. Due to the overall diversity and number of setups, it is difficult to assess the total number of establishments linked to this segment.

Raw material in this sector is in the form of gemstones and gold found in abundance in the northern region, which is mined and transported to cutting and polishing units established nearby. These polished, cut or unpolished stones are either exported or sold to the local market where it is used in jewelry manufacturing. This sector, however, lacks updated technology to process/polish these gems as well as sophisticated mining techniques to ensure good quantity and quality. With strong financial support and introduction of state of the art technology, this sector has huge potential for phenomenal growth.

5.1.1 Market Sizing and Lending Potential

As mentioned before the gem sector is relatively unorganized while the jewelry sector is comparatively more organized. It is, therefore, hard to avail data for the number of units established. Precious raw gems and gemstones segment is located in the Gilgit-Baltistan, AJK, and KPK while jewelry manufacturing and retail cluster has highest concentration in the urban cities like Karachi and Lahore. The following table provides the registered establishments in both gemstones (**Table D**) and jewelry (**Table E**) segment separately, which is an estimate as exact data is not available.

Table D: Cluster Locations 'Precious Raw Gem and Gemstones'	
Area	No. of Establishment
Peshawar	406
Swat	22
Rawalpindi	22
Lahore	16
Islamabad	15
Abbottabad	9
Mardan	6
Nowshera	4
Skardu	3
Gilgit	3
Faisalabad	3
Quetta	2
Karachi	2
Others	60
Total	573

Table E: Cluster Locations 'Jewelry Manufacturing'	
Area	No. of Establishment
Karachi	309
Lahore	256
Quetta	34
Faisalabad	16
Others	3
Total	618

Source: Corporate Development Partners

5.1.2 Segment Demographics

Demographic information is obtained from industry sources and primary research conducted using a selected sample of businesses in major cities of Pakistan. 'Gemstones and Jewelry' manufacturing is spread out in the Gilgit-Baltistan and KPK and urban cities of the country respectively. The locations of customers indicated by the graph below (**Figure 5.1-b**) are pertaining for those businesses that have been covered in the surveys. Peshawar and Rawalpindi mostly pertains to the 'Gem and Jewelry' sector while Karachi and Quetta mostly cover the jewelry manufacturing and retail outlets.

More than half of the businesses (52%) have been in operation for more than 10 years while 20% have been in operation for 5 to 10 years, which indicates that business owners have long experience of running their business (**Figure 5.1-a**).

Figure 5.1-a: Number of years in operation

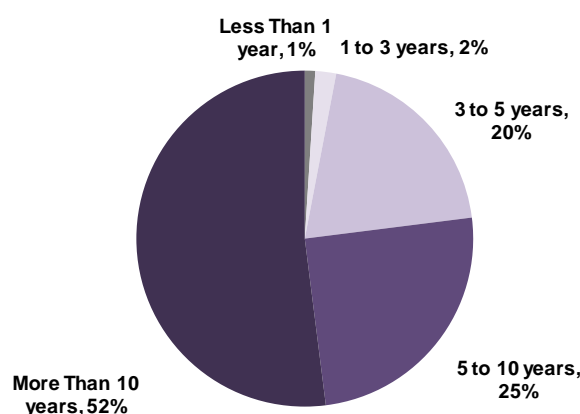
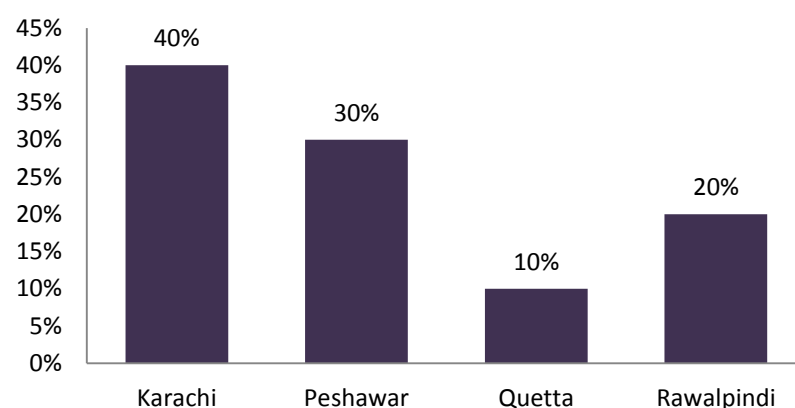


Figure 5.1-b: Customers' presence within the country



Source: Survey Findings

5.2 Owner Profile

The business owners in almost half of the businesses (49%) consist mainly of people in the age group of 31-40 years while 42% of the owners are between the ages of 41-50 years (**Figure 5.2-b**). Almost half (52%) of the businesses have been established for more than 10 years. This indicates that the business owners are well experienced and have been in this business for many years with sound knowledge of the industry. 57% of the business owners in the survey have completed their bachelor/college with only 1% not having had any education at all (**Figure 5.2-a**). About 60% of the businesses have large set ups, with 10-24 employees (**Figure 5.3-c**). Predominantly 75% of the businesses are individual/proprietorships being run by family members. 18% of these businesses have been formed on partnership basis (**Figure 5.2-d**).

Figure 5.2-a: Education level of business owners

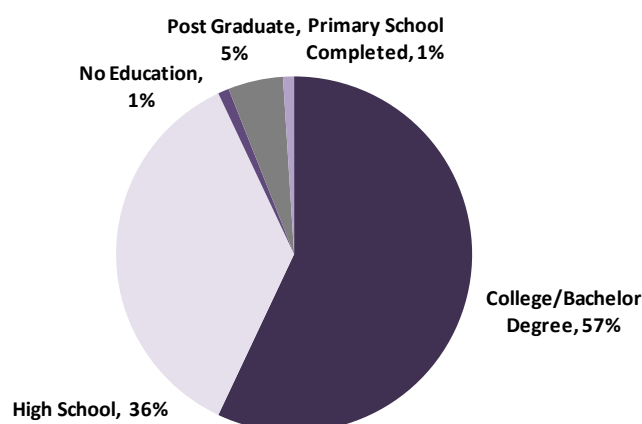


Figure 5.2-b: Age group of business owners

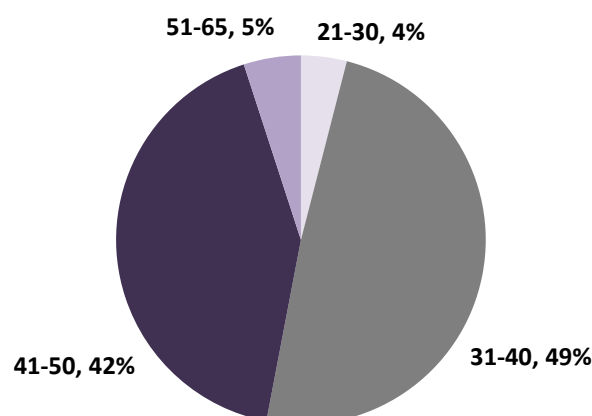


Figure 5.2-c: Number of employees under business owners

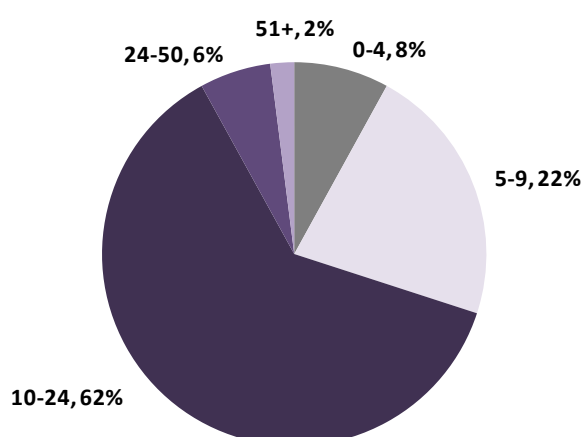
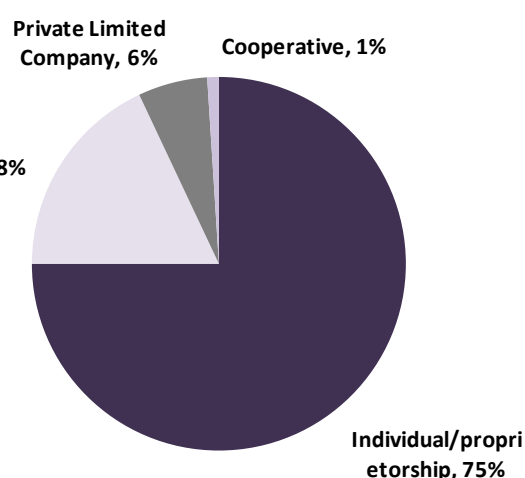


Figure 5.2-d: Ownership type



Source: Survey Findings

5.3 Business Linkages

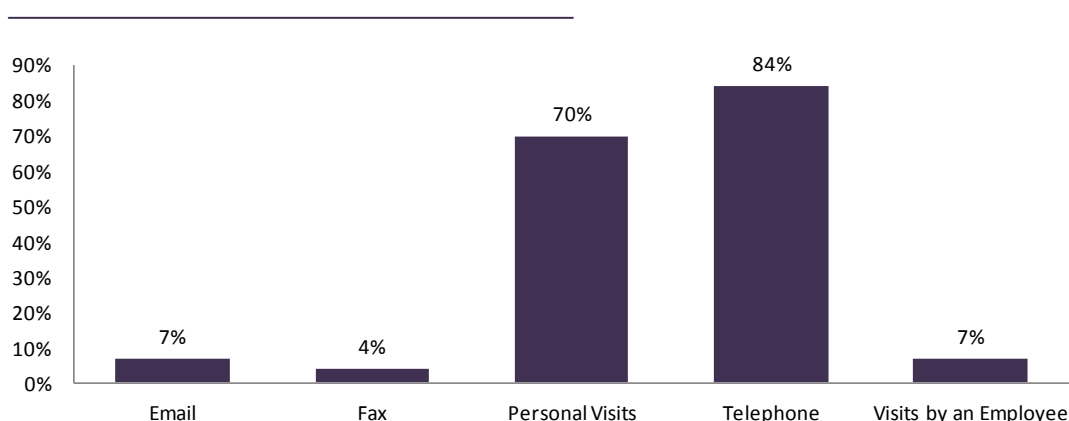
Businesses in the segment are connected to various institutions, which are directly or indirectly affected by the business operations, primary stakeholders and their interests are enlisted in the following table (**Table F**):

Table F: Stake Holders and Their Interests

Gem and Jewelry Sector	
Stakeholder	Interest
Owners	Growth and access to finance
Suppliers	Better terms, lower risk of payment defaults and maintaining consistent quality
Customers	Product quality, reasonable pricing and timely delivery
Financial Institutions	Lending products and increase in deposits
Government	Economic growth, employment and favorable regulations for export of finished goods, establishment of training institutes

Businesses employ various mediums as means of communication with their customers (**Figure 5.3-a**) however, personal visits by customers and telephone are widely utilized by 84% and 70% of the customers respectively. In 7% of the cases employees pay direct visit to the retail shops for collection of the order. The businesses in this sector operate in competitive environment with businesses mostly having more than 10 competitors.

Figure 5.3-a: Communication with customers



Source: Survey Findings

Source: Survey Findings

Major raw material for Jewelry manufacturing includes gold and gemstones. Jewelry retail and manufacturing units store inventory/stocks for sale mainly in the form of gold, the quantity of which varies for different owners depending on the size of their setup. Following are the raw materials used in this sector (**Table G** and **Table H**):

Table G: Raw Material for Precious Raw Gemstones Sector

Diamond Powder
Carborundum Powder
Aluminum Oxide
Tin Oxide
Cerium Oxide
Grinding Laps
Precision Drill

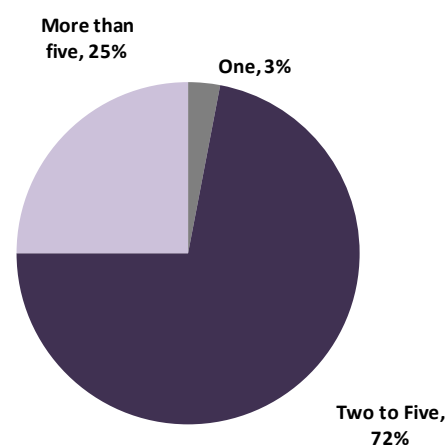
Table H: Raw Material for Jewelry Manufacturing Sector

Casting Rubber
Nitric Acid
Investment Powder (Plaster)
Detergent
Coloring Chemicals

Raw material in the gemstones segment are gems in raw form, mostly for export purposes. Many of those raw gems are smuggled which results in further depletion of profit. Some of these gems are however, transported to the jewelry manufacturing market in the urban cities.

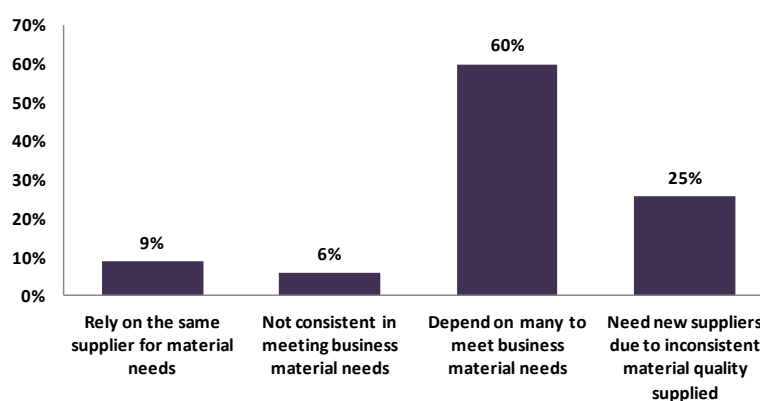
60% of the businesses depend on many suppliers to meet their inventory needs with only 9% depending on the same suppliers for years (**Figure 5.3-c**) which depicts difficult availability of material needs when required. 6% of the businesses however are not consistent in their suppliers to meet their raw material needs while 25% of the businesses need new suppliers due to inconsistent quality of stock supplied. About 72% of the businesses rely on two-five suppliers to meet their raw material needs (**Figure 5.3-b**).

Figure 5.3-b: Number of Suppliers



Source: Survey Findings

Figure 5.3-c: Supplier Relationship



5.4 Business Cycle

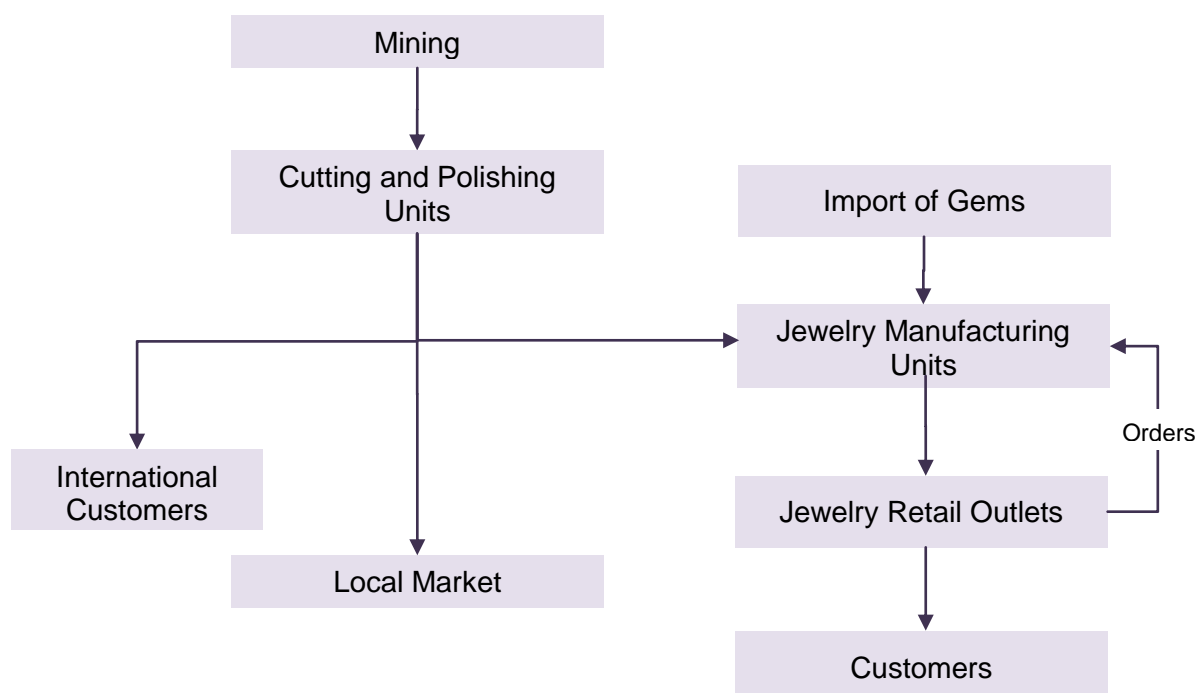
This sector is not seasonal although the overall demand tends to increase during wedding seasons. These seasons are mostly in winter and spring. The requirement for traditional jewelry rises immensely with huge orders being placed. This becomes challenging for jewelers at times to be able to complete the orders in time.

These orders are placed in retail shops which either have in-house jewelry manufacturing or have outsourced this function (**Figure 5.4-a**). The jewelry manufacturing cluster includes many units being specialised in various processes including polishing and crafting units being dependant on each other.

The gemstone sector includes mining activity and units which specialise in cutting and polishing these gems. These units then either export these precious stones in raw form or after polishing them. Many are however smuggled especially by unregistered mining units. Due to lack of technology, many jewelry manufacturing units import polished and cut gems of better quality.

The businesses in this sector are affected by the energy crises prevailing in the country, like almost every other sectors, where the use of machinery is required. Outdated technology is another major issue faced by this sector. Law and order situation in the country further hampers the production as well as demand due to security and protection reasons.

Figure 5.4-a: Business Model



5.4.1 Working Capital

Working capital is dependent upon payment terms offered to customers and received from suppliers. Businesses in 'Gem and Jewelry' sector operate by having local and overseas contracts with the customers.

The repayment periods provided by the suppliers are mostly (45%) within one month (*Figure 5.4-c*). 11% of the businesses claimed in the interview of receiving repayment period of two months from their suppliers. 49% of the businesses do not provide any credit to their customers (*Figure 5.4-b*) while 40% give credit for one month to their customers. The direct cash or cheque payment is usually the advance which is taken at the time of placing an order while credit period pertains to the remaining amount which is paid after the completion of those orders.

It shows from the following two graphs that the businesses in this sector have similar supplier and customer credit terms, which indicates a relatively smooth working capital cycle. The finished goods however, may have a long shelf life. Many businesses therefore operate with just-in-time approach.

Figure 5.4-c: Repayment Terms from Suppliers

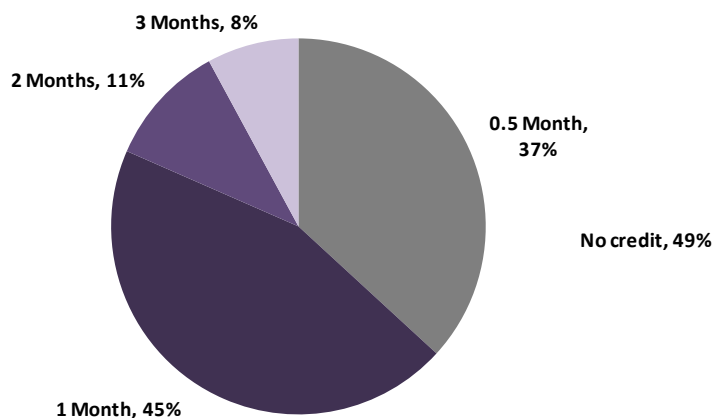
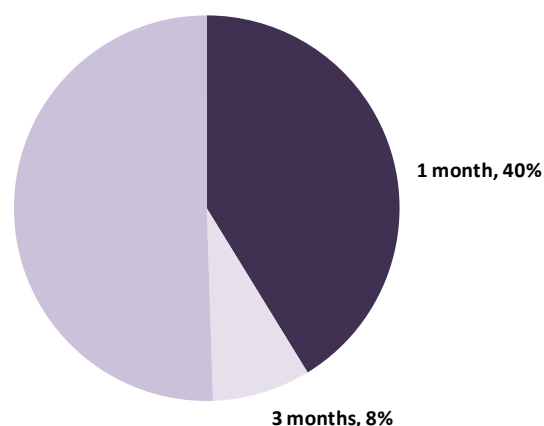


Figure 5.4-b: Repayment Terms to Customers



Source: Survey Findings

5.5 Financial Assessment and Profile

Almost all of the businesses in this segment claim to prepare Financial Statements from which, however, more than half of the business owners do not have their financial statements audited.

Half of the business owners keep track of accounts themselves, while the rest hire accountants, finance managers, secretaries or general managers to manage their accounts. More than half of these businesses do not issue printed sales invoice to their customers while some do not receive sales invoice from their suppliers either.

A rough estimate was given by the business owners regarding business assets employed, annual revenue, income and expenses.

Business owners' reluctance for sharing financial information presents an issue for calculation of segment's accurate benchmark financial ratios. The following table (*Table I*) provides key financial ratios of this sector which have been calculated on the average value of the financial range provided to us by the businesses covered in the survey. These ratios are an estimate at best and cannot be utilized to assess the performance of the businesses prevailing throughout this sector.

Table I: Sector Financials Snapshot

Financial Information	PKR
Business Assets	24,720,000
Total Revenue	90,000,000
Annual Expense	80,000,000
Total Income	10,790,000
Key Financial Ratios	
Profit Margin	12%
Operating Expenses/ Revenue	88%
Asset turnover	3.64 times
ROA	43.6%

Conclusively, a low capital investment compared to the business's revenues especially in the jewelry manufacturing segment. This mostly pertains to gem segment as it is mostly unorganized with almost no updated technology, depending on old blasting techniques. Despite a high return on assets, the expenses are also high which results to a lower net income for average businesses in this sector.

5.6 Financial Information

Primary survey findings reflect the Revenue, Expenses, Income and Capital Expenditure under the selected sample for the sector.

Liabilities constitutes of trade payables while total assets comprise of plant and machinery, land and building, inventory/stock, trade receivables and IT equipment. Survey findings demonstrate 76% businesses are operating with total assets between PKR 10-50 million, while the remaining operate with assets less than PKR 10 million (**Figure 5.6-a**), suggesting low initial capital required to set up the business. A low total asset value may also pertain to the use of outdated technology and low inventory level maintained by the businesses in this sector.

Plant and machinery constitutes of IT equipments which are used for grading the stones and gold. Other machinery includes polishing, cutting and carving machines. 35% of the business owners in the 'Gem and Jewelry' sector incurred capital expenditure in the past five years (**Figure 5.6-b**).

Figure 5.6-a: Business Assets

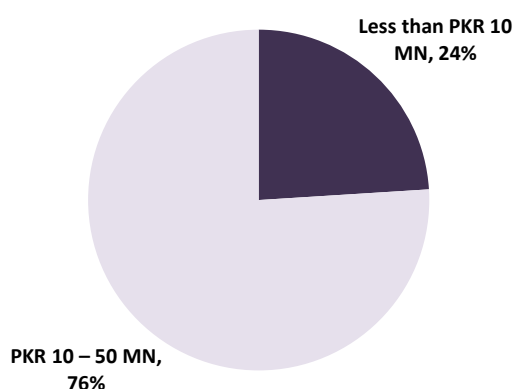
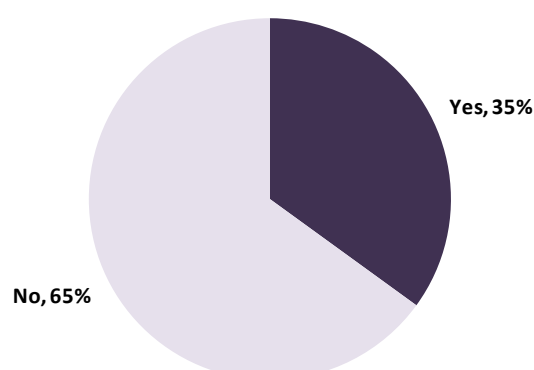


Figure 5.6-b: Capital Expenditure



Source: Survey Findings

Annual average revenue is predominantly between PKR 10-50 million and more than PKR 100 million throughout the sector, with percentages being 50% and 41% respectively (**Figure 5.6-c**). Expenses primarily represent material and employee cost. The expenses are between PKR 10-50 million for half of the businesses while for 38% it is more than PKR 100 million (**Figure 5.6-d**).

Figure 5.6-c: Total Revenue

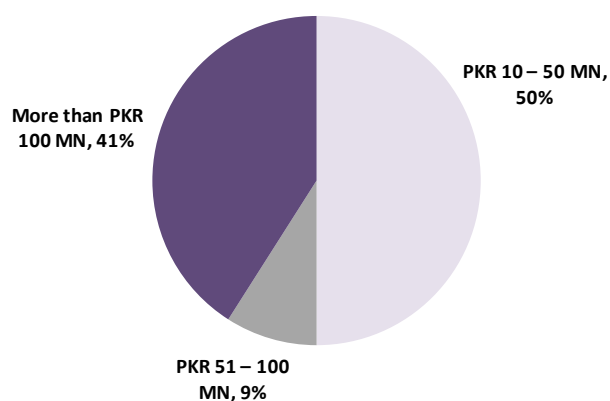
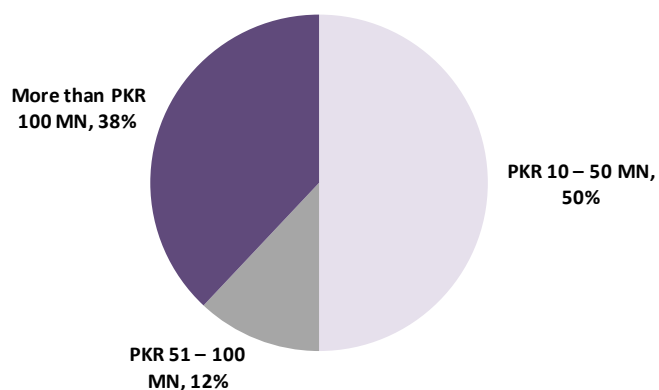


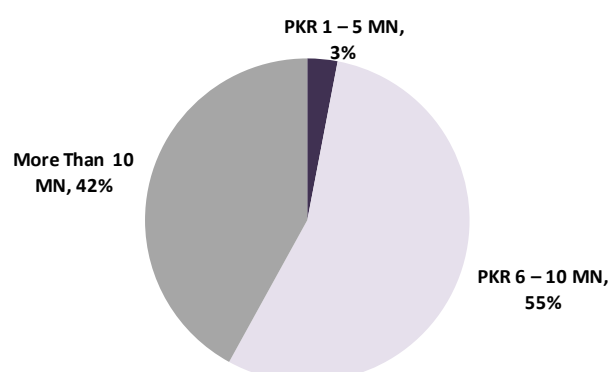
Figure 5.6-d: Annual Expense



Source: Survey Findings

55% of the businesses have disclosed to earn between PKR 6-10 million while 42% claim to earn more than PKR 10 million of average income for the last three years (**Figure 5.6-e**). 3% of the business owners show earnings in the range of PKR 1-5 million annually. Overall the earnings of the businesses in this sector is moderate.

Figure 5.6-e: Total Income



Source: Survey Findings

5.7 Indicative Business Requirements

The following table (**Table J**) lists the business equipment required by the businesses in the 'Gem and Jewelry' sector. The values provided below are susceptible to volatility in market prices. In addition, individual business owners will have distinctive requirements as per their business needs and their size. The table below is neither comprehensive nor specific and provides only an indication as to the typical requirement for set up or the expansion needs of a small sized business within this segment.

Table J: Indicative Equipment Requirement	Cost PKR (per unit)
<u>Jewelry Manufacturing Requirement</u>	
Polishing Machine	5,000 – 30,000
Silver/Gold Plating Machine	30,000
Wax Casting Machine	100,000
Gas Furnace	500,000
Die Press Machine	50,000
Wire Making Machine	150,000
Tools set <i>(Depending on number of pieces)</i>	10,000
Caste Machine <i>(Depending on size)</i>	15,000 – 200,000
<u>Gemstones Requirement</u>	
Trimming machine	100,000
Calibrating machines with wheels	250,000
Dual Edge Grinding Machine	200,000
Buffing, Sanding & Polishing Machines	200,000
Saw Faceting Machine	100,000

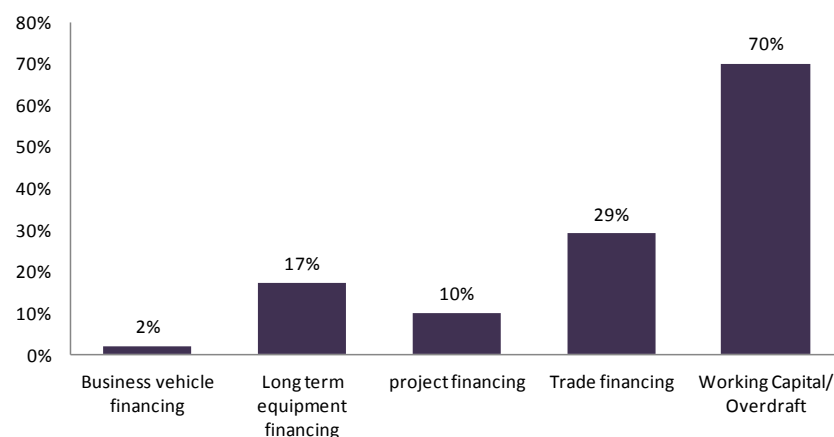
5.8 Financial Need Analysis

More than half of the business owners themselves are in charge of their business funds. The funds are mainly required for working capital/overdraft in 70% of the businesses interviewed from which 41% of the businesses requiring working capital finance for letter of credit (LC) to import raw material. This pertains to those businesses in jewelry sector who import gold and gemstones because of higher quality and easier availability for some. 27% of the businesses require finance for finished goods.

Amongst the business assets, buildings followed by machinery and equipment was required by the business owners with percentages resting at 66% and 47% respectively (**Figure 5.8-b**).

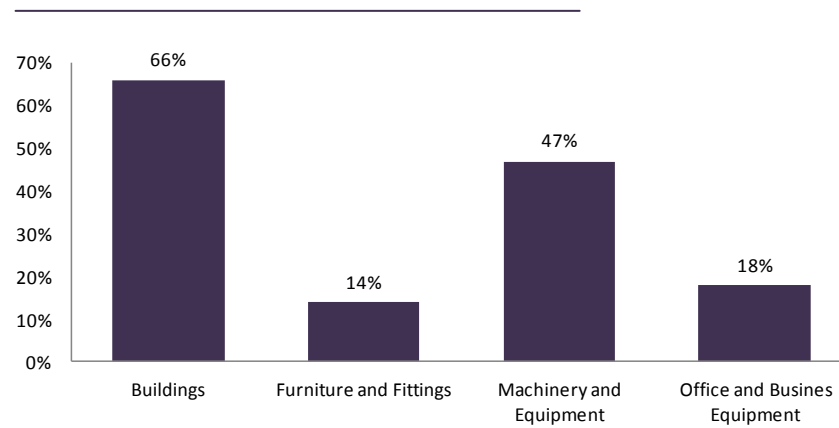
Almost half of the businesses show reliance on banks while some also depend on their own savings as their source to fund their business needs. Few also use cashflows from their business as their source of funds. Working capital financing can provide the SMEs in the segment to assist them in their inventory and expansion of their business, as indicated by 70% of the businesses (**Figure 5.8-a**).

Figure 5.8-a: Business Funding Needs



Source: Survey Findings

Figure 5.88-a: Fixed Assets Financing Requirements



Source: Survey Findings

5.9 Usage of Banking Products

Very few owners are aware of SME segment specific efforts made by the Government of Pakistan; however, businesses in this sector have shown interest in potential loan products and availed it from banks but for those who did not avail cited religious issues and high interest rate as their reasons for not availing loan. The most used loan products were business loans and vehicle financing (loans, leasing arrangement) by 78% and 43% of the businesses respectively.

More than half of the business owners listed the key driver in choosing a certain bank being convenience/location/proximity to business and efficient and rapid service. Few owners were keen to propose feature or product they wished to be offered by the bank which were, better online services, more sme specific products and free payorder services.

Other services such as cash management and money transfer facility are used by the businesses in this sector with percentages resting at 91% and 10% respectively. 6% of the businesses also availed payroll services from banks.

56% of respondents do not use any insurance products; 21% of the businesses have travel insurance, followed by 19% availing office equipment insurance. The remaining few percentage have legal insurance (6%), medical aid (7%) and motor vehicle insurance (4%). 4% also have their inventory insured. None of the business owners showed any interest in availing any insurance product if provided by banks as they prefer to avail such products directly from insurance companies.

The sector consist of 37% of the businesses who avail advisory services from which only 19% claimed to pay for it. Majority of them avail advisory services from family, friends and relatives with 57% of them being satisfied with their current source of advisory services. 27% of the business owners are willingly to pay for such services if provided by the banks as they believe them to have more experience in finance. This area provides opportunity for banks to target this sector.

Banking Product	Usage Percentage
Deposit (Checking) Account	69%
Term Deposits	37%
Loan Products	37%

5.10 Segment Risk Considerations

This sector shows the potential of phenomenal growth in Pakistan but is still highly unorganized with outdated technology and therefore is embedded with many risks. Following are the risks that pertains in this sector.

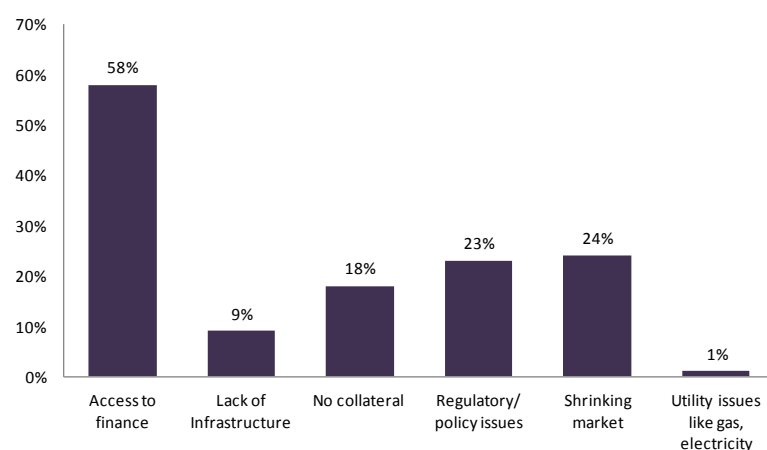
Businesses in the segment are largely individual proprietorships with majority of the business owners having this business as their only source of income. Ironically, more than half of the businesses in this sector listed scarce raw material as a risk to their business. This can be due to old mining methods and hardly any latest gem polishing and cutting machinery available. This forces the manufacturing units to import these gems. This is followed by risk of non-repayment of loans from banks by 55% of the businesses. Inflation is also considered as one of the primary risk of the business owners.

80% of the businesses address these risks through more capital investment. 20% of the businesses also focus on inventory management (**Figure 5.10-b**). Almost half of the businesses operate from rented premises and so incur fixed expenses in the form of montly rent payments of their premises.

More than half of the businesses do not have their Financial Statements audited. Further, many of the business owners do not issue printed sales invoice to their customers or receive sales invoice from their suppliers, as mentioned above. This may pose serious miscalculation in accounts and incomplete accounting records.

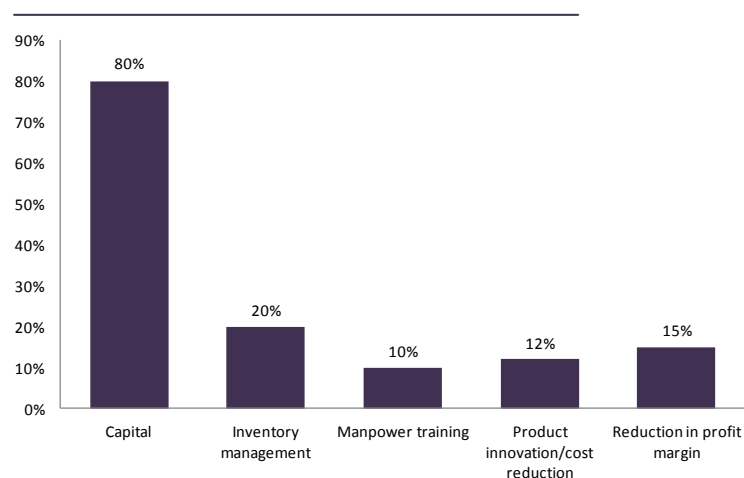
A large proportion of SMEs in the segment do not use any insurance products. One of the major restraint to business expansion listed is lack of access to finance (58%) which presents opportunities for the banks to target these businesses (**Figure 5.10-a**).

Figure 5.10-a: Business Expansion Restraints



Source: Survey Findings

Figure 5.10-b: How Business Risk Addressed



Source: Survey Findings

Following are the strengths and weaknesses inherent in this sector:

Strengths

- High capacity for phenomenal growth
- High demand in both local and international market
- Low initial capital
- Availability of skilled labor
- Establishment of training institutes
- Recognition in the global market
- Availability of raw materials specially gems and semi-precious stones

Weaknesses

- Unorganized infrastructure
- Energy crises
- Lack of Knowledge of international market
- Lack of innovation
- Export and smuggling of gems in raw form
- Law and order situation

Further, the risks inherent to the segment include:

- Inconsistent supply of inventory
- Unaudited financial statements of many businesses
- No proper book keeping
- Outdated technology

Possible Mitigating Factors:

- Lending only to those businesses which have been operating for more than five years
- Proposing products to business with a verifiable banking history of more than two years
- Review of accounts and register of invoices
- Registration of property documents
- Product quality certificates

6 Proposed Banking Product Suite

6.1 Product Features

Based on our primary and secondary research we propose the following for growth of '*Gem and Jewelry*' sector:

Asset Products:

- Working capital/overdraft Finance Facility
- '*Gem and Jewelry*' Machinery Leasing
- Industrial Power Generator Leasing
- Export Finance

Liability Products:

- Business Bank Account

Other products

- Banc assurance
- Branchless Banking (Mobile)
- Utility Bill Payment

Table K: Working capital / Overdraft Finance Facility	
Particular	Details
Initial deposit	Minimum initial deposit of PKR 10,000
Tenure	1 year with no requirement of Annual Cleanup for principle amount. However, regular payment of markup is must for renewal of limit.
Loan Limit	<ul style="list-style-type: none"> • Minimum Limit - PKR 5,000,000 • Maximum Limit - PKR 50,000,000 • Minimum and maximum loan limits are reviewed annually <p>Total loan limit offered will not exceed an average six months of usage determined over a period of the last three years</p> <p><i>(Maximum limit is set based on 50% mark-up of average revenue estimated for this sector)</i></p>
Documentation	One time documentation (as required by banks) for a period of three years
Repayments & Withdrawals	<ul style="list-style-type: none"> • Flexible repayment conditions: lump sum payment on the due date or partial repayments • Multiple withdrawals are allowed during the tenure of loan
Cleanup	Borrower is liable to clear the entire loan amount, both principal and markup, once in a year on a date indicated by the borrower & mutually agreed by the bank.
Markup	As per prevailing KIBOR and spread
Markup charges	Mark up will be charged only on the amount utilized by the borrower
Renewal	Renewal will be on the basis of fresh application, subject to clearing of entire loan amount including markup and satisfactory credit history
Penalty	No early repayment penalty may be imposed on the borrower (subject to banks discretion)
Insurance	Mandatory insurance as per SBP guidelines
Security	Raw material stock. Mortgage of business premises for those who operate from owned premises.

Table L: 'Gem and Jewelry' Machinery Leasing	
Particular	Details
Down Payment	Minimum down payment of 20%
Salient Features	<ul style="list-style-type: none"> Equipment & machinery leasing will be provided for expansion capital only to businesses who have been operating for 3 or more years A list of pre-approved equipment and machinery manufacturers will be developed based on information received from trade association and market sources Disbursement will be made directly to pre-approved equipment and machinery vendors for supply of equipment to the borrower
Tenure	3 - 5 years
Loan Limit	<ul style="list-style-type: none"> Minimum Limit - PKR 500,000 Maximum Limit - PKR 10,000,000
Documentation	<ul style="list-style-type: none"> One time documentation required for a period of three years Financial Statements
Repayments & Withdrawals	Repayments will be based upon preset Equal Monthly Installments
Markup	As per prevailing KIBOR and spread
Penalty	As per existing bank policies and cost of charges
Insurance	Mandatory insurance as per SBP guidelines
Security/Collateral	5% of invoice as security deposit. Security as per requirement and satisfaction of the bank

Table M: Industrial Power Generator Leasing	
Particular	Details
Down Payment	Minimum down payment of 20%
Salient Features	<ul style="list-style-type: none"> • Loan amount will be directly transferred to suppliers' accounts against invoices • Credit facility will be offered directly through pre-approved generator suppliers
Tenure	3-5 years
Documentation	<ul style="list-style-type: none"> • Business Financial Statements • Proof of business operation for last three years
Loan Limit	<ul style="list-style-type: none"> • Minimum Limit - PKR 500,000 • Maximum Limit - PKR 10,000,000
Repayments & Withdrawals	Repayments will be based upon present Equal Monthly Installments
Markup	As per prevailing KIBOR and spread
Insurance	Mandatory Insurance facility as per SBP guidelines
Penalty	As per existing bank policies and cost of charges

Table N: Export Refinance	
Particular	Details
Initial deposit	Any form of collateral/guarantee which the bank feels fit.
Tenure	Depends on the contract terms of LC
Documentation	One time documentation required for a period of one year which may include financial statements, company incorporation documents etc.
Markup	As per the yearly revised rate provided by the State Bank of Pakistan
Penalty	As per the yearly revised rate provided by the State Bank of Pakistan
Insurance	Mandatory insurance as per SBP guidelines
Security	As per the requirement and satisfaction of bank.

Table O: SME Business Bank Account	
Particular	Details
Account Type	Non- remunerative Current Account
Documentation	CNIC/smart NIC, completion of KYC requirements as per SBP Regulations
Facilities	<ul style="list-style-type: none"> • Cheque Book • Upgraded ATM facilities • Business Visa Debit Card • Phone Banking • Mobile Banking • Internet Banking • Monthly account statement

Table P: Other Products	
Particular	Details
Banc assurance	Bancassurance products such as Business Premises Insurance, Personal Injury Insurance, Equipment and Vehicle insurance can be proposed by banks through its channels offering reasonable rates and servicing through banking channels such as direct debit
Branchless Banking (Mobile)	Mobile banking services for instance balance check, bill payment and funds transfer
Utility Bill Payment	Service for easy payment of electricity, gas, telephone and cell phone bills

6.2 Eligibility Criteria for Asset Products

Table Q: Asset Products Criteria

Indicators	Description
Borrower Eligibility Analysis	During assessment of customers, take into account the total indebtedness of the potential borrower, his disposable income and ensure that the total financing to customer does not exceed the prescribed limits as laid down in approved policies of bank. Borrower should be in business of ' <i>Gem and Jewelry</i> ' for the past three years and hold a valid CNIC/smart NIC.
Business Analysis	To assess the Borrower's position, verification of their revenues can be verified by the bank. Business premises ownership documents should be verified against name of the owner.
Credit worthiness	Credit worthiness of the borrower may be ascertained by collecting information from e-CIB or other credit information bureaus.
Financial parameters	To assess average expenses, income generated and repayment capacity of the borrower.
Adherence to Lending Standards	To assess that Customer/ Borrower requirements are in compliance with standards set for revolving finance scheme by the Bank and/ or Regulatory Authorities.
Banking History	Verifiable banking history of more than one year with active accounts
Business Operations	Business should be in operation for more than three years. If the business is involved in exporting their finished goods then they should be involved in export business for the last 3 years.
Trade body membership	Business should be a member of the sector's trade body.

7 Distribution and Communication Considerations

SMEs in '*Gem and Jewelry*' are spread out in the Gilgit-Baltistan and KPK of the country in gem sector while jewelry manufacturing sector are mostly scattered in the urban areas with the biggest cluster in Karachi and Lahore. The banks will therefore have to reach further to be able to reach and target the unorganized gem sector.

7.1 Marketing Objectives of Banks

Marketing objectives for building and promoting the brand image of SME Products for '*Gem and Jewelry*' sector are as follows:

- Educate and create awareness for financial needs and banking products in the identified market regions
- Develop strategies to attract a large number of owners in '*Gem and Jewelry*' sector to avail banks' lending/financial products such as conducting seminars with All Pakistan Commercial Exporters Association and All Pakistan Gems Merchants and Jewelers Association at cluster locations of Gems and Jewelry sector
- Increase direct interaction of Relationship Managers with '*Gem and Jewelry*' units and retail shops to promote more direct and close interaction with the business owners and to assist small businesses in navigating difficult economic and business conditions
- Provide sponsorships for trade fair and exhibitions of '*Gem and Jewelry*' which not only promotes the sectors competency but also links the promotion of bank's brand image locally and worldwide

7.2 Promotional Activities by Banks

To create awareness of SME specific products in the target market, the banks may aggressively advertise their banking products through various promotional programs and events:

- Conduct workshops in coordination with All Pakistan Commercial Exporters Association of Rough & Unpolished Precious and Semi-Precious Stones (APCEA) and Pakistan Gems and Jewelry Development Company (PGJDC)
 - To provide more interaction to business owners with trade associations
 - To enhance communication between them regarding industry specific issues.
- Organize promotional events in cluster locations of both gem and jewelry to build strong image of the bank among the target audiences

Banks can service this segment through the following proposed channels: *(Please note that this list is not exhaustive)*:

- Direct Sales Agents
- Tele Sales
- Trade association backed seminars
- Branches in cluster locations
- Identify opportunities for expansion through market sources
- Involvement in trade fairs and exhibitions

7.3 Distribution Strategy for Banks

As primary means of customer service and sales interaction, distribution channels play a central role in the customer relationship process, which further increases growth. Banks' challenge is to improve and integrate their multiple distribution channels to consistently deliver an enhanced experience and foster better customer relationships. Top priority is placed in attracting and retaining customers within and across these channels.

To reach maximum percentage of target market, Banks need to have a comprehensive distribution strategy. Banks should aim to cater banking needs of 'Gem and Jewelry' sector through its products on national basis in major cities of the country where jewelry manufacturing units are located and then further target gemstones polishing and cutting units located in the Gilgit-Baltistan, KPK and AJK.

Banks may adopt following conventional channels for distribution:

- **Branches:** Establishment of lending branches in 'Gem and Jewelry' cluster regions with a potential to attract large number of customers.
- **Direct Sales Agent:** This activity may be outsourced and a trained marketing team should periodically visit identified areas within the cities, to educate potential customers and create awareness of the products and services being offered under SME Products Suite.
- **F2F interactions:** A deeper level of interaction may provide an integrated customer focus, by relationship managers involved in face to face interaction, which will become critical in helping better communication for product awareness and in addressing hesitations faced by the business owners.

Following Technology based alternate delivery channels can also be adopted for distribution

- **Internet Banking:** With technology up gradation mobile phones have become sophisticated and capable of handling advanced applications and services, so banking via mobile phones appeal to consumers on multiple fronts.
- **Short Message Service (SMS):** Marketing team can send out mass messages in Urdu or English to 'Gem and Jewelry' segment for advertising bank's products.