INFRASTRUCTURE, HOUSING & SME FINANCE DEPARTMENT

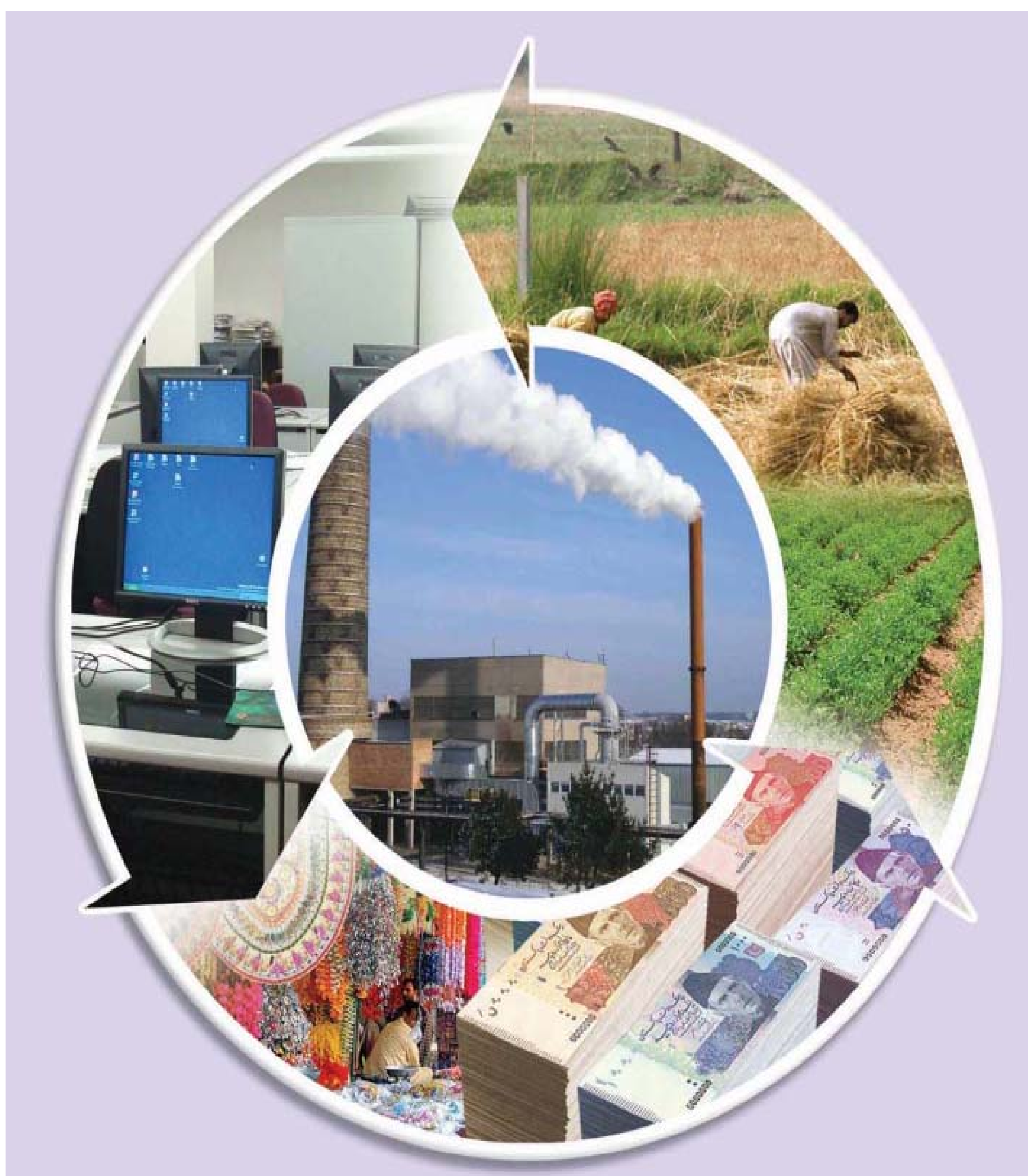
State Bank of Pakistan

JUNE 2011

Development Finance Quarterly Review

SPECIAL POINTS OF INTEREST:

- **SME Finance**
- **Microfinance**
- **Agri. finance**
- **Housing finance**
- **Infrastructure finance**
- **SBP Refinance Schemes**
- **SBP Policy Initiatives**
- **Global News**
- **Special Section on nexus between financial inclusion and financial integrity**
- **DF Outlook**



THE REVIEW TEAM

Mr. Syed Samar Hasnain	(samar.husnain@sbp.org.pk)	Team Leader
Mr. Allauddin Achakzai	(allauddin.achakzai@sbp.org.pk)	Member
Mr. Karim Alam	(karim.alam@sbp.org.pk)	Member

ACKNOWLEDGEMENT

DFG Review Team appreciates and acknowledges contributions of the Departments and individuals of Development Finance Group, State Bank of Pakistan for their valuable reviews and analysis.
Moreover, we are also thankful to the following officials for their invaluable contributions.

Mr. Muhammad Ishfaq (Team Leader), S M Hafeez

Mr. Imran Ahmed (Team leader), Syed Farrukh Ali, Mr. Usman Shaukat

Mr. Qazi Shoaib Ahmad (Team Leader), Ms. Fouzia Aslam, Mr. Shahbaz Shahid

Mr. Muhammad Imaduddin (Team Leader), Syed Ali Raza

Contents

Contents 1
Executive Summary 2
1.1. SME Finance 3
1.2. Outstanding Amount- Break-Ups 3
1.3. Number of borrowers 5
1.4. Non-performing loans 6
1.5. Banking group wise distribution 6
1.6. SME cluster profiling- Survey findings 8
1.7. SBP Refinance Schemes 10
1.7.1. Export Finance Scheme (EFS) 10
1.7.2. Banking Group-Wise Utilization of EFS 10
1.7.3. Commodity Wise Distribution of EFS 11
1.7.4. Borrower Wise Distribution of EFS Fund 11
1.7.5. Regional Allocation of Borrowers 12
1.7.6. Islamic Export Refinance Scheme (IERS) 12
1.7.7. Long-Term Financing Facility (LTFF) 12
1.7.8. Refinance Scheme for Flood Affected Areas 13
2.0. Microfinance 14
2.1. Advances – Growth, Up-Scaling and Quality 14
2.2. Alternate Delivery Channels (ADCs) 15
2.3. Assets Growth 16
2.4. Funding Structure 16
3.0. Agricultural Finance 18
3.1. Introduction 18
3.2. Agricultural Credit Disbursement 18
3.3. Province-wise Disbursement 20
3.4. Agri. Non-Performing Loans 21
3.5. Number of Agri. Loan Borrowers 22
4.0. Housing Finance 23
4.1. Gross Outstanding 24
4.2. Non-Performing Loans 25
4.3. Number of Borrowers 26
4.4. Share of Banks 27
4.5. Disbursements 29
4.6. Sectoral Share 29
4.7. Housing Finance Business of Micro Finance Banks 30
4.8. Analysis of Loan Variables adopted by Banks/DFIs & HBFC 30
5.0. Infrastructure Finance 33
5.1. Outstanding Portfolio 33
5.2. Disbursements 33
5.3. Analysis of Sectoral Share in Infrastructure Finance Portfolio 34
5.4. Banking Sector-wise Disbursements 35
5.5. Banking Sector-wise Share in Outstanding 35
5.6. New Initiatives 35
6.0. Key Development Finance Initiatives – Policy and Industry 36
7.0. Development Finance news from around the World 41
8.0. Special Section – Nexus between financial inclusion and financial integrity 43
9.0. Development Finance - Outlook 48
Development Finance reviews published by SBP 49

Executive Summary

Heavy rains, energy shortages, and deteriorating law & order situation continued to pose stress on the domestic economy during the quarter. These developments were mirrored in the weakness in net lending to most development finance segments during the quarter ending June 30, 2011 (**Table 1**).

Table 1: DFG Wise Break up of Outstanding Amount (Rs. Billions)

Outstanding	Jun-10		Mar-11		Jun-11		Change	
	Amount	%Share	Amount	%Share	Amount	%Share	QoQ	YoY
SMEs	318.8	38.7	303.0	36.0	292.5	35.4%	-3.5%	-8.2%
Agriculture	164.1	19.9	164.9	19.6	169.2	20.5%	2.6%	3.1%
Microfinance (MFBs Only)	10.1	1.2	10.7	1.3	13.5	1.6%	26.7%	33.8%
Housing Finance	70.3	8.5	65.4	7.8	61.6	7.5%	-5.8%	-12.4%
Infrastructure Finance	260.0	31.6	296.5	35.3	290.0	35.1%	-2.2%	11.5%
Total	**823.4**	**100.0**	**840.6**	**100.0**	**826.9**	**100.0%**	**-1.6%**	**0.4%**

On an annual basis, disaggregated data shows a more mixed picture; while SME finance, and Housing loans continued to decline, Agriculture credit, Microfinance and Infrastructure finance all recorded positive growth. The decline in aggregate DF loans is owed to both demand and supply factors. On the supply side, banks' risk appetite remained subdued, particularly given the opportunity offered by aggressive government sector borrowings. Similarly, demand was constrained by prevailing unfavorable economic conditions.

During the quarter, in contrast to a 0.6 percent decline in the number of total banking sector borrowers, the number of DF borrowers rose by 7.1 percent. The rise in the number of DF borrowers, even as the quantum of outstanding loans saw a small decline. This implies a relatively strong growth in small loans during the period. Encouragingly this holds true, even if the microfinance loans (that are typically very small) are excluded, i.e. the quarter saw a jump in small agriculture loans. If this represents the beginning of a trend, it bodes well for the future.

Similarly, while the total NPLs of the banking industry rose by 1.1 percent during the quarter, NPLs in DF sectors declined by 0.8 percent to Rs 162.5 billion. Of the total NPLs of DF Sectors, SME had 59.2 percent, Agri. Sector 22.3 percent, and the remaining 18.5 percent related to other DF sectors. The decline DF NPLs largely reflect restructuring of banks SME portfolios.

1.1. SME Finance

At the end of Jun-11, SME sector's outstanding credit stood at Rs. 292.5 billion constituting about 8.2 percent of total outstanding banking portfolio (corporate, SME, agriculture, consumer, commodity and others). This was 3.5% lower than the previous quarter and 2.3% lower than the corresponding period in 2010. A decline in NPLs of SMEs by 4.8% (QoQ) shows that further rise in NPLs has stopped reflecting both, adoption of better risk mitigation techniques by banks and restructuring of older inflected portfolios. Credit stream to SMEs has been declining since 2008 (after the liquidity crunch in Q4-2008) as banks being risk averse are observing greater due diligence while extending credit to SMEs and thus are diverting funds towards less risky commodity operation of the government as well as investing in T-bills. In addition, high interest rates, rising inflation, energy shortage, and gradually increasing energy costs have also diminished the demand for bank credit by SMEs. Resultantly, number of borrowers in SME sector declined by 1.9% QoQ at the end of Jun-11.

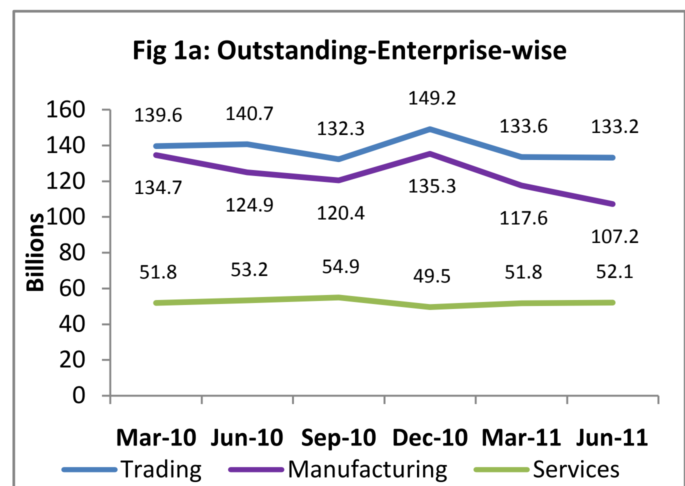
An enterprise-wise analysis revealed that share of trading SMEs in total SME loans outstanding was 45.5%, m*anufacturing SMEs'* share was 36.7%, and *services* SMEs 17.8% at the end of the period under review. Moreover, their respective share in the total SME borrowers was 50.6%, 12.2%, and 37.2%, indicating largest average loan size in manufacturing sector.

There has been a swell in NPLs of the overall banking industry during the last couple of years and this quarter, too, saw a rise of about 1.1%. However, at the end of the period under review, NPLs of SME sector declined by 4.8% on QoQ basis, defying the overall trend, mainly due to restructuring of a major private bank in which commercial and SME accounts were converted into retail & middle market accounts thus affecting SME sector.

1.2. Outstanding Amount- Break-Ups

Enterprise wise

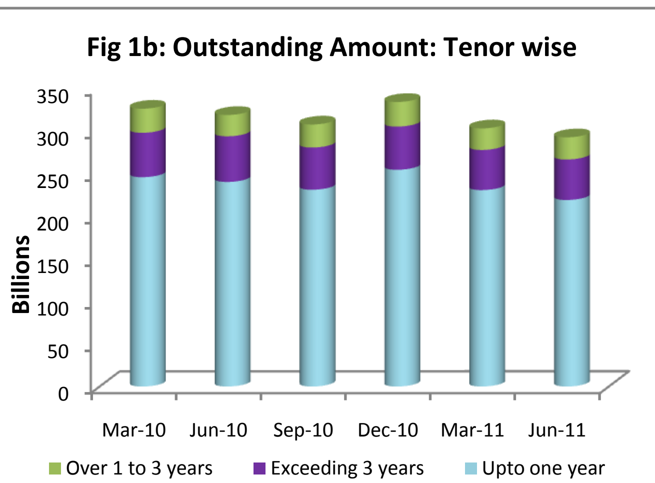
An enterprise-wise break-up, at the end of Jun-11, reveals that the fall in outstanding amount was mainly driven by a fall in lending to manufacturing sub-sector. In contrast, services sub-sector showed resilience as outstanding amount under this sub-sector posted a rise of 0.6% on QoQ basis. However, this meager rise in services sub-sector could not offset the impact of fall in the other two sub-sectors.



It is important to note that a decline in lending to trading and manufacturing is mainly attributed to the decrease in short term advances like export finance for SMEs Part-I and working capital for SMEs (other than SBP schemes) during this period.

Tenor wise

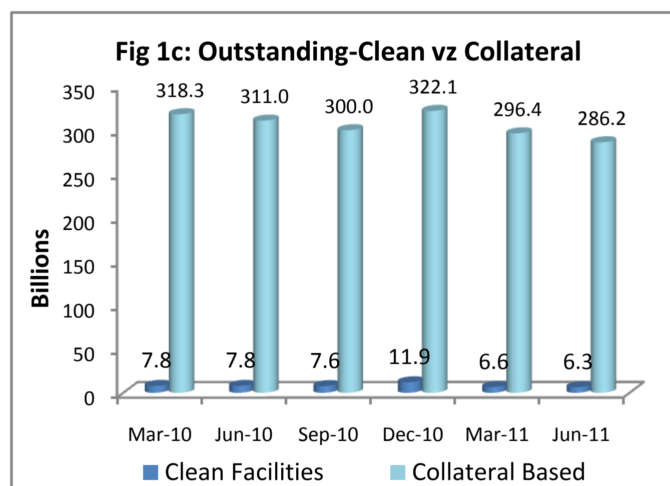
At the end of Jun-11, the tenor-wise breakup of the total SME outstanding loans showed that the dominant share of about 74.8%, following the usual trend, was availed by SMEs under the category of *short term* financing (up to one year), while the share of l*ong* and me*dium* term financing was 16.3% and 8.9% respectively. At the end of the period under review, SME financing for all tenors improved relative to the preceding quarter, except the Short term financing which saw a decline of 5.1% on QoQ basis.



It is evident from **Figure 1b** that the major chunk of the financing continues to be under short term financing as SMEs require funds more frequently to stabilize cash flows from operations. This is also consistent with the substantial share of financing for working capital.

Clean vs Collateral

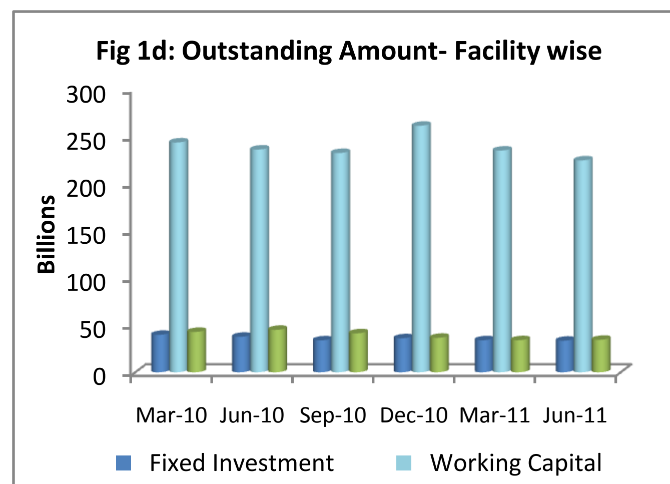
At the end of Jun-11, an analysis of SME outstanding amount viz-a-viz **clean** and **collateral** revealed that the major chunk of financing (97.8%) was made against collateral while only 2.2% of the amount was provided to SMEs under clean lending category- **Figure 1c.**



The meager share under clean lending reflects (a) the banks mindset of relying on security/collateral while lending to SMEs (b) a lack of innovative products and borrower evaluation techniques whereby borrowers' repayment capacity is judged through business/cashflows assessment instead of asset/collaterals.

Facility- wise

An analysis of facility-wise breakup, at the end of June 2011, exhibited that the share of working capital in outstanding SME amount was 76.8%. The remaining financing was almost equally shared by fixed investment and trade related loans (**Figure 1d**).



To achieve a rapid and sustainable growth of SME sector, there is a need to encourage SMEs to increase fixed investment with the introduction of risk mitigation measures and increased availability of credible sector information as well as the introduction of innovative financing products by both traditional and Islamic banks. Morever, these would need to be complemented by the government initiates to ensure a more conducive business environment (particularly resolution of energy shortages).

Size- wise

At the end of the period under review, a size- wise loan breakup (**Table 1A**) exhibits that the major chunk, about 68.0%, in total SME Outstanding portfolio was availed by SMEs against the bracket size of loans of over Rs. 5 million. While the share of SMEs against the bracket size of loans up to Rs. 1 million was about 9.8%.

Table 1A: Outstanding Amount: Loan Size wise Breakup (Rs. Billions)

Breakup	Mar-10	Jun-10	Sep-10	Dec-10	Mar-11	Jun-11	% Share (Jun-11)
Advances up to 0.5 Million	22.0	21.2	20.0	18.4	16.9	15.8	5.4%
Advances over 0.5 to 1 Million	11.9	12.9	12.6	13.2	13.0	12.7	4.4%
Advances over 1 to 2 Million	20.4	21.4	20.8	21.6	21.1	20.6	7.1%
Advances over 2 to 3 Million	17.0	17.9	16.3	16.3	16.4	16.0	5.5%
Advances over 3 to 5 Million	29.2	30.5	28.5	30.4	28.5	28.4	9.7%
Advances over 5 to 10 Million	50.6	52.4	51.7	55.7	51.4	50.4	17.2%
Advances over 10 to 20 Million	50.0	50.5	48.6	54.9	52.2	48.5	16.6%
Advances over 20 Million	124.9	112.0	109.1	123.6	103.7	100.0	34.2%
Total SME	**326.1**	**318.8**	**307.6**	**334.0**	**303.0**	**292.5**	**100.0%**

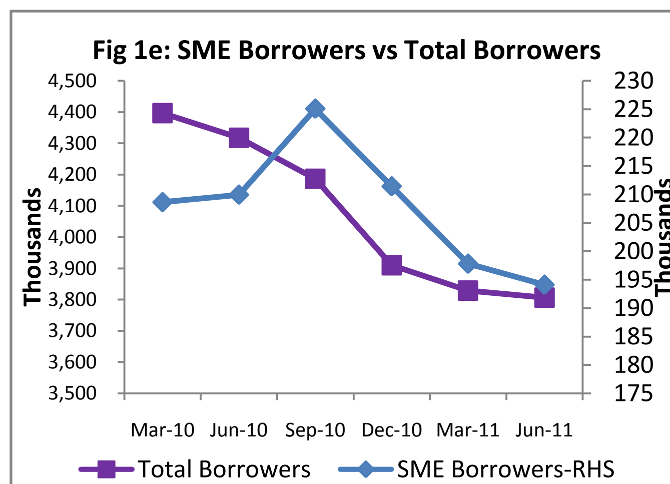
It is interesting to note that while all loan categories witnessed a decline in outstanding amount at the end of Jun-11 (QoQ), category of advances of over Rs. 50 million, which formed about 13.2% in total SME outstanding amount, registered an increase of 4.3%.

1.3. Number of borrowers

At the end of the period under review, all sub sectors of the economy saw a decline in their number of borrowers except the Agri. and commodity financing which saw a rise of 5.2% and 7.0 % respectively on QoQ basis.

Total number of SME borrowers stood at 194,110 constituting about 5.1% of the total number of outstanding borrowers of the banking industry. Thus recorded a decline of about 1.9% QoQ basis compared to a rise of 0.6% during the corresponding period in 2010 (**Figure 1e**). It is a source of concern that the decline in number of SME borrowers is comparatively higher than the overall reduction of 0.6 % in the number of borrowers of total banking industry.

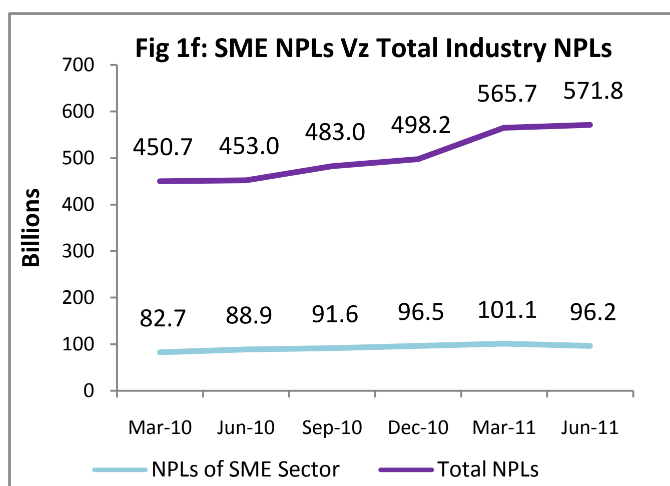
Of the total SME borrowers, about 89.0% availed working capital finance, 5.0% fixed investment, and 6.0% trade finance. Similarly, the the share of the borrowers categorized as *trading SMEs* was the highest with 50.6%, followed by *services SMEs* with 37.2% and *manufacturing SMEs* with 12.2% at the end of the quarter under review.



Likewise, an analysis of *loan size* wise borrowers manifest that 50.2% of total SME Borrowers fell under the bracket size of *up to Rs. 0.5 million* followed by over *Rs. 0.5 to 1 million and Rs. 1 to 2 million with* a share of 8.5*%, 8.0, r*espectively. Moreover, about 77.6% of the total SME borrowers availed advances of up to Rs. 5 million.

1.4. Non-performing loans

Unpredictably, defying the overall trend of rising NPLs the non-performing loans (NPLs) of SME Sector decreased from Rs. 101.1 billion at the end of Mar-11 to Rs. 96.2 billion at the end of Jun-11, low by 4.7%. Moreover, as a result of the rise in NPLs of the overall banking sector vs decline in SME NPLs, share of SME NPLs in total NPLs dropped from 17.9% in Mar-2011 to 16.8% by Jun-11.



The decline in NPLs of SME Sector is principally due to restructuring of loan portfolio of a major private bank whereby commercial and SME accounts were converted into retail & middle market accounts thus affecting corporate and SME sectors.

1.5. Banking group wise distribution

At the end of the period under review, the share of *public sector banks***,** i.e., NBP, FWBL, BOP, BOK, and Sindh bank constituted 13.3% of the total SME outstanding amount **(Table 1B**); slightly lower than the 13.4 % recorded in the preceding quarter. Their NPLs of SME sector saw a slight increase from Rs. 17.3 billion (17.1%) to Rs. 17.4 billion (18.1%) on QoQ basis.

At the end of Jun-11*, Private Banks (19 institutions)* share in total SME loans outstanding was 81.9%, following a 3.5 percent decline in the portfolio during the quarter. This represented about 9.5% of their overall outstanding

loans. Moreover, unlike the trend for public banks, the SME NPLs of private sector banks declined by 6.5% on QoQ basis, largely representing restructurings in the SME loan portfolio of one private bank.

Table 1B: Banking sector wise distribution- as of Jun-11

Category	**% Share of SME in**			**% Share in Total**			**Quarterly Change**		
Bank	Total O/S Amount	Total O/S Borrowers	Total NPLs	SME O/S	SME Borrowers	SME NPLs	SME O/S	SME Borrowers	SME NPLs
Public	5.5%	6.5%	10.6%	13.3%	32.9%	18.1%	-4.0%	-0.7%	0.5%
Specialized	8.5%	4.3%	22.1%	3.3%	19.8%	8.1%	0.3%	-0.4%	-1.1%
Private	9.5%	5.0%	20.4%	81.9%	46.9%	72.8%	-3.5%	-3.2%	-6.5%
Islamic	3.6%	2.4%	8.5%	1.1%	0.3%	0.7%	-3.7%	-5.0%	6.5%
Foreign	0.8%	0.1%	3.9%	0.2%	0.0%	0.3%	4.3%	1.1%	2.4%
DFIs	0.5%	0.9%	0.5%	0.1%	0.0%	0.1%	-3.3%	-13.6%	13.5%
Banks	8.3%	5.1%	17.3%	99.9%	100.0%	99.9%	-3.5%	-1.9%	-4.8%
Total	**8.2%**	**5.1%**	**16.8%**	**100.0%**	**100.0%**	**100.0%**	**-3.5%**	**-1.9%**	**-4.8%**

Islamic banks' outstanding amount, at the end of Jun-11, was about Rs. 3.5 billion, constituting about 1.1% of the total SME outstanding amount. This category of banks witnessed a quarterly decline of 3.7% and 5.0% in SME outstanding amount and borrowers respectively. However, their NPLs recorded a rise of 6.5% at the end of the period under review. The low share of Islamic banks towards SME Sector is primarily due to the fact that the major chunk (92.0% as on Jun-11) of overall portfolio is occupied by corporate and consumer sectors. However, given a sizeable share of trade related financing in SME sector, enormous opportunities for expansion for the Islamic banks are available in this segment.

Specialized banks category consists of SME Bank, ZTBL, PPCBL and IDBP. The absolute outstanding amount of this category saw a slight increase from Rs. 9.75 billion as of Mar-11 to Rs. 9.68 as of Jun-11, constituting about 3.3% of total SME financing. Their portfolio has been hovering around Rs. 10 billion for the last few years and did not witness any significant improvement. However, it is encouraging that NPLs of this group saw a decline of 1.1% on a QoQ basis.

This quarter, too, did not see any significant improvement in the negligible share of *foreign banks'* and *DFIs* in total SME finance. The lackluster performance of these Financial Institutions thus, suggests that these institutions in particular and banks in general need to recognize the significance of priority sectors in terms of a huge untapped market.

Banks need to take innovative measures, besides building their capacity, in order to target the SME market in an effective way. When assessing comparatively small and straightforward business applications, banks may largely

rely on standardized credit scoring techniques and also centralizing/rationalizing business-banking operations may significantly reduce processing costs. Additionally, standardized computer-based assessments may also be more accurate and transparent than relying on personal judgments. As a result, banks may be able to offer more loans, faster and in larger amounts besides reducing previously high security requirements.

It is imperative to note that a vibrant SME sector would help sustain strong economic growth that would support future growth of the overall financial sector.

1.6. SME cluster profiling- Survey findings

State Bank of Pakistan, like a central bank in any developing country, 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 assists the process of economic growth and promotes the utilization of the country's resources.

SME cluster profiling project was implemented by IFC, in collaboration with SBP and in consultation with major banks in Pakistan. The objective is to provide critical information to the banking industry so that SMEs are catered with a responsible, profitable and sustainable manner. Below mentioned section presents selected information concerning *Manufacturing Segment-Grain Mill Products and Animal Feeds* (http://www.sbp.org.pk/departments/ihfd-ifc.htm), based on primary findings of the survey exercise conducted in major cities of Pakistan.

Manufacturing Segment-Grain Mill Products and Animal Feeds

Key Impediments

The segment remains largely unbanked owing to the following key impediments:

- A different risk profile, lack of substantial collateral, conservative approach adopted by financial institutions and Lack of awareness and willingness by banks for lending to this key SME sub-segment

Sampling Plan

- In total, interviews with 27 SME owners were conducted for Grain Mill Products and Animal Feeds segment.

Demand

- Animal feed industry has not yet developed to any sizeable extent in Pakistan. Feed is a major cost, of about 70% in livestock and dairy farming and its demand is continually increasing.
- Most of the farmers about 75% have small land holdings on which most of the livestock population is concentrated. With growing trends towards the establishment of structured and corporate dairy cattle and buffalo farms in semi-urban areas of Pakistan, there is a substantial requirement of high quality animal feed.
- The nutrients available under the present pattern of feed utilization do not meet the requirements of Pakistan's existing livestock population. There is comparatively poor nutrient composition of indigenous feed ingredients due to differences in varieties and use of improper soil fertilizers.
- Grain Mills is an organized segment which faces consistent demand throughout the year. It has strong export demands; however, unluckily their products are sold at low prices.

Supply

- Research indicates that Pakistan has 215 feed mills, but only a few are preparing compound feed for livestock. Approximately 40 million tones of crop residues are produced annually in Pakistan of which 22% is contributed by wheat and 53% by rice. The industry is currently working under 70% of its installed capacity.
- Due to lack of proper storage facility, various agricultural products when produced have quite high moisture content and become liable to be affected with insect damage, auto-oxidation and fungal contamination.
- There are approximately 915 wheat mills all over Pakistan with the milling capacity of 77,275 million. tones daily. However due to economical and political situation, the country has faced serious flour shortages in recent years. Rice Milling is a comparatively steady business with consistent supplies in the market.

Future Prospects

- Investment in dairy and livestock sector is increasing day by day and quality feed is a pre-requisite in profitable dairy and livestock farming. However there is a dire need of investment in animal feeds as this industry is so vital for the growth of livestock through good quality feeds.
- Grain Mills industry is showing steady improvement, however a lot depends on the economic and political situation of the country.

Demography

- The grain mills products and animal feeds segment is mostly dispersed in Punjab and few areas in Sindh near to poultry farms.
- The segment predominantly consists of small and medium size enterprises which operate on costly machinery and labor intensive model, with few still using outdated technology
- Cluster location data was unavailable for these sub- segments from trade bodies and other secondary and tertiary sources

Owners Profiles

- The business owners consist mainly of people in the age groups of 31-40 years and 41-50 year
- Majority of businesses are run on partnership basis, which accounts for 56%. Further, businesses predominantly are run by families, and preferring family members to undertake organizational functions

Financial Need Analysis

- Financial requirements mainly centered on machinery and equipment of the business
- The Grain mills sub-segment is generally more open to banking products and is keen on obtaining financing. While Animal Feeds sub-segment is underserved with respect to financing and banking products, the businesses owners are not inclined towards obtaining finance, however their interest may develop if banking products are more specific and suited to their needs.
- 22% respondents do not pay for any of the proposed insurance products and 48% of them are not interested in availing any insurance product in future.

Usage of Banking Products

- Nearly 36% of the segment is currently paying for some kind of advisory service provided by their banks
- Around 14% feel that banks will have high service charges.

Proposed Banking Products

- Based on primary and secondary research the following products have been proposed, for social and economic growth of the segment:
  - **Asset Products:** Overdraft/Revolving Finance Facility
  - **Liability Products:** Business Bank Account
  - **Other Products:** Bancassurance, Branchless Banking (Mobile), Utility Bill Payment

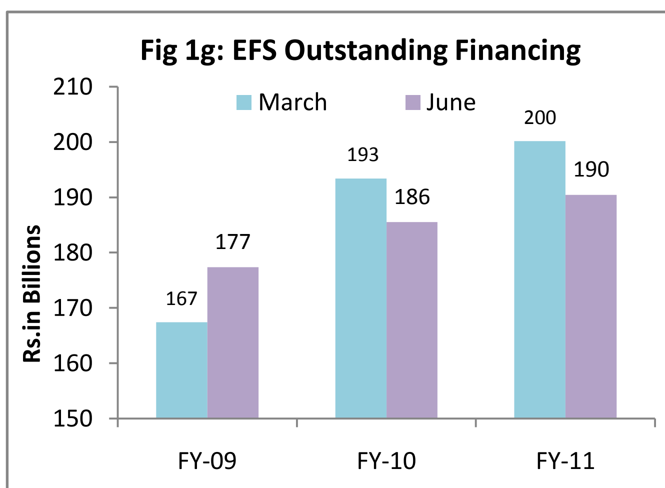
1.7. SBP Refinance Schemes

State Bank of Pakistan is continuously in the process of improving its Refinance Schemes to facilitate the exports oriented sectors and boost long term investment in industrial sector. The schemes are aligned to the market needs for bridging the gaps of working capital requirements of exporters through Export Finance Scheme (EFS) and building capacity of export oriented industry for SMEs and others through Long Term Financing Schemes viz Long Term Financing Facility (LTFF), Refinancing Facility for Modernization of SMEs, Financing Facility for Storage of Agricultural Produce (FFSAP) and Scheme for Financing Power Plants Using Renewable Energy.

In order to address issues of carpet industry, performance level of hand knotted carpets exporters for FY 2010-11 was reduced from 2 times to 1.5 times during the quarter under review. SBP extended the scope and validity of the Refinance Scheme for Revival of Small and Medium Size Enterprises (SMEs) and Agricultural Activities in Flood Affected Areas. Moreover, SBP declared plant and machinery of producing such packaging material eligible under LTFF Scheme, which is exclusively used in packaging/preservation of food items. On release of budgetary allocation by the Ministry of Textile Industry SBP reimbursed 2nd Installment of mark-up rate subsidy for six months ending Aug-10, to the exporters / borrowers of Textile Industry.

1.7.1. Export Finance Scheme (EFS)

Outstanding financing under EFS decreased by 5.0% from Rs.200 billion to Rs.190.5 billion as compared to previous quarter. This decrease is mainly due to the closing period of financial year for financing under EFS Part-II.



In this period exporters having availed finance under EFS Part-II usually focus on realization of their exports proceeds instead of availing additional finance, to match the performance requirements and avoid short-performance as the performance of exporters under EFS Part-II for a financial year is measured on the basis of exports proceeds realized up to 30th June each year. Commodity and borrower wise financing under EFS continued to show skewed distribution. Only textile sector hold 63.0% share of the total credit extended under the scheme, while out of 1,698 borrowers, top 300 availed about 87.0% of the total financing.

1.7.2. Banking Group-Wise Utilization of EFS

The Private Sector Banks remain the major participant in the Export Finance Scheme with highest share of Rs.161 billion (85.0%) in the outstanding, followed by Public-sector banks with Rs.14 billion (7.0%).
Compared to previous quarter, a major decrease in outstanding of Rs.10 billion is exhibited in private sector banks.

Table 1C: Banking Group Wise Outstanding Position of EFS				
Banking Group	June-11	March-11	June-10	Δ YoY
		(Rs in Billions)		%
Public Banks	13.5	13.0	10.7	26.3%
Private Banks	161.4	171.0	162.7	-0.8%
Islamic Banks	7.4	7.0	4.5	62.4%
Foreign Banks	8.1	9.0	7.6	7.8%
Total	**190.5**	**200.0**	**185.5**	**2.7%**

1.7.3. Commodity Wise Distribution of EFS

The commodity-wise outstanding financing of Rs. 190 billion shows textile sector at the top with Rs. 119 billion (63.0%) followed by edible goods with Rs. 26 billion (14.0%). Both the sectors showed decrease of 5.4% and 4.8% respectively when compared to Mar-11 quarter due to cautious behavior of exporters under EFS Part-II to match performance against the already availed loans. Metal Products, Carpets and Sports Goods showed an increase of 9.2%, 18.3% and 8.3% respectively over the previous quarter due to overall increase of exports of these sectors during the quarter under review.

Table 1D: Commodity Wise Outstanding Financing under EFS (Rs. Billions)					
Sector	June-10	Mar-11	June-11	% Change	
		Billion PKR		YoY	QoQ
Textile/Textile Products	115.0	126.2	119.3	-3.8%	-5.4%
Edible Goods	26.7	27.1	25.8	3.4%	-4.8%
Leather/Leather Goods	10.8	11.6	11.7	-8.3%	0.4%
Machinery	1.4	1.4	1.4	2.5%	-4.2%
Metal Products	3.0	2.1	2.3	23.6%	9.2%
Carpets	2.8	1.7	2.1	27.2%	18.3%
Sports Goods	2.8	2.7	2.9	-1.5%	8.3%
Other Commodities	23.0	27.3	25.0	-8.8%	-8.2%
Total	**185.5**	**200.1**	**190.5**	**-2.7%**	**-4.8%**

1.7.4. Borrower Wise Distribution of EFS Fund

During the 4th quarter of FY-11, the total number of borrowers under Export Finance Scheme (EFS) stood at 1,698 with an average loan size of Rs.112 million. A nominal decrease of 0.4% was recorded in total number of borrowers during the quarter under review as compared to previous quarter.

Region-wise Allocation of EFS Funds

About 94.0% of total EFS funds are concentrated in four major cities i.e. Karachi, Sialkot, Lahore and Faisalabad. However, there is an extensive disparity in terms of utilization of EFS funds from one region to another. For

instance, Karachi & Sialkot have almost equal in terms of total number of borrowers, but the total EFS financing in Karachi stands at 47.0% *(Rs. 89.8 billion)* of total financing, whereas the same is only 5.0% *(Rs.10.3 billion)* in Sialkot. Further inconsistent patterns have been witnessed with regard to average loan size and number of borrowers across the regions. For instance, the average loan size at Rawalpindi is Rs.487 Million, in Karachi the same is at Rs.176 million, while it is just Rs.19 Million per borrower in Sialkot. The smaller loan size in Sialkot is mainly due to the existence of a large number of Small Business Enterprises that are involved in manufacturing and exporting Sports goods, Surgical Instruments and Leather products.

1.7.5. Regional Allocation of Borrowers

No change was observed in region-wise allocation of EFS Borrowers. According to banks' data for the quarter ended Jun-11, up to 89.0% of borrowers still exist in the above mentioned four major cities, where only Karachi & Sialkot has about 62.0% of total beneficiaries with both sharing 30.0% and 32.0% respectively. There were just 3 borrowers at Rawalpindi at the end of Jun-11.

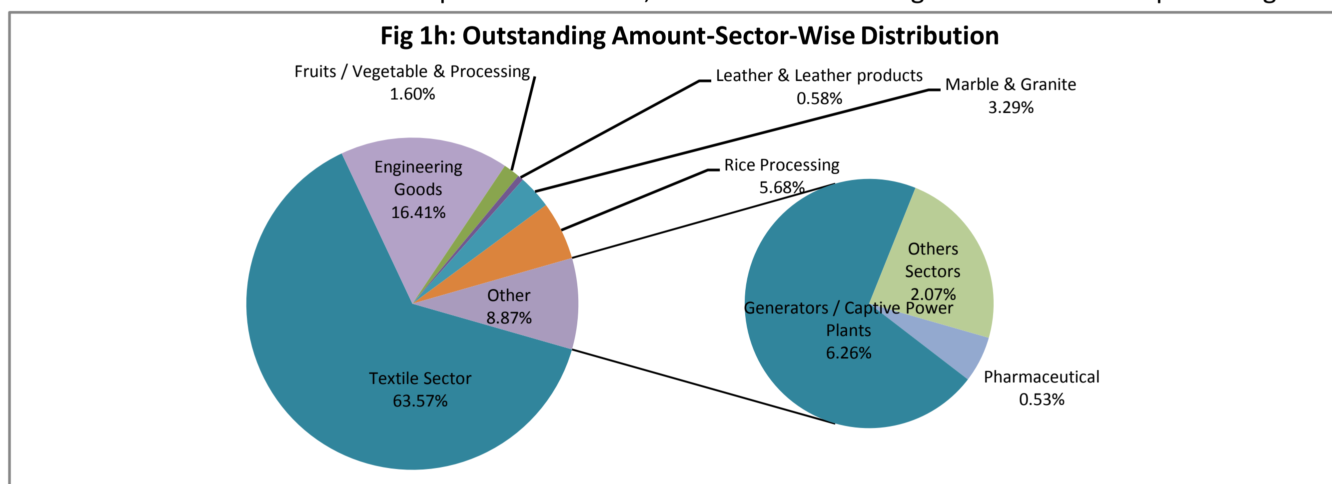
1.7.6. Islamic Export Refinance Scheme (IERS)

During the quarter under review, the total numbers of participating banks were 11 (4 Islamic Banks, 6 Conventional Banks' Islamic Banking Operations and 1 Foreign Islamic Bank). The limits assigned under the scheme were increased by 34.0% (to Rs.31.4 billion from Rs 23.4 billion in Jun-11), due to overall expansion in Islamic mode of financing portfolio of conventional banks resulting from allowing increased maximum cap for IERS under their EFS limit. Out of total limits Rs. 12.7 billion has been allocated to Islamic Banks and remaining Rs. 18.7 billion to Islamic Banking Branches of Conventional Banks. The total IERS financing outstanding at the end of the quarter stood at Rs. 15.4 billion, which increased by 5.0% from Rs. 14.7 billion in previous quarter.

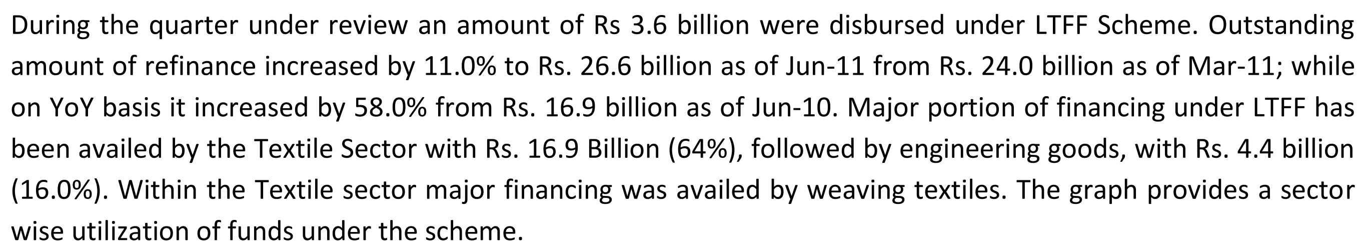
1.7.7. Long-Term Financing Facility (LTFF)

LTFF Scheme is one of the most important Schemes, which has been designed to facilitate export led growth

Fig 1h: Outstanding Amount-Sector-Wise Distribution



through setting up export oriented projects. Under the Scheme funds on long term basis (up-to 10 years) are provided for procurement of imported and locally manufactured plant & machinery. In order to meet the demand of export oriented projects, the limit of banks/DFIs for the 4th quarter were increased from Rs. 19,500 million to Rs. 19,770 million.



During the quarter under review an amount of Rs 3.6 billion were disbursed under LTFF Scheme. Outstanding amount of refinance increased by 11.0% to Rs. 26.6 billion as of Jun-11 from Rs. 24.0 billion as of Mar-11; while on YoY basis it increased by 58.0% from Rs. 16.9 billion as of Jun-10. Major portion of financing under LTFF has been availed by the Textile Sector with Rs. 16.9 Billion (64%), followed by engineering goods, with Rs. 4.4 billion (16.0%). Within the Textile sector major financing was availed by weaving textiles. The graph provides a sector wise utilization of funds under the scheme.

During the quarter, adjustments of Rs. 2.2 billion were made under LTF-EOP (defunct scheme), and the outstanding position of LTF EOP as on Jun-11 stood at Rs. 16.2 billion. Thus, the total long term financing outstanding under LTFF and LTF-EOP stood at Rs. 42.8 billion as of Jun-11.

1.7.8. Refinance Scheme for Flood Affected Areas

During the quarter under review, SBP expanded the scope and extended the validity of above Scheme with a view to improve access to finance for SMEs and farmers in the flood affected areas. Now the scheme will also provide financing to the non-farm sector. Earlier, the financing under the scheme was allowed to farm sector only. Likewise, SBP has also allowed banks/DFIs to repay the principal amount of refinance within 15 days of the due date(s), instead of 7 days. The validity of the scheme has been extended to November 30, 2012 from 31st October, 2011.

2.0. Microfinance

During the quarter, the recently augmented microfinance banking sector has witnessed escalation in almost all key indicators including advances, deposits, portfolio quality, funding and outreach of the sector. Importantly, number of active borrowers increased by 14.0% mainly due to inclusion of NRSP borrowers. The increase in market share of MFBs due to NRSP MFB is expected to persist in next quarter.

On the positive note, growth in advances and deposits (Table 2A) was contributed by all nation-wide MFBs during the quarter. The portfolio quality remarkably improved during the quarter. The current quarter's PAR at 3.7% indicates that the rise in NPLs in last two quarters triggered by devastating flood of the second half of 2010 finally seems to settle down. Besides recovery of flood affected loans, other factors contributing in improved portfolio quality were reimbursement received on account of Malakand relief package, and the bigger GLP base. On the other hand, the two district-base MFBs continue to be characterized by perpetual reduction in loan portfolio & operations, and high NPLs.

Table: 2A ***Amount in Rs. '000'**

Outreach	Jun-10	Mar-11	Jun-11	Growth		
				(YOY) %	(QoQ)%	
Borrowers	667,268	624,896	713,563	7%	14%	↑
Advances *	10,113,502	10,677,662	13,523,748	34%	27%	↑
NPLs*	260,787	568,594	505,431	94%	-11%	↓
PAR >30 Days in %	2.58%	5.33%	3.74%	45%	-30%	↓
Deposits*	8,122,596	8,901,277	11,167,174	37%	25%	↑
Assets*	18,754,256	20,667,506	26,471,237	41%	28%	↑
Equity*	5,279,341	5,615,400	6,364,125	21%	13%	↑

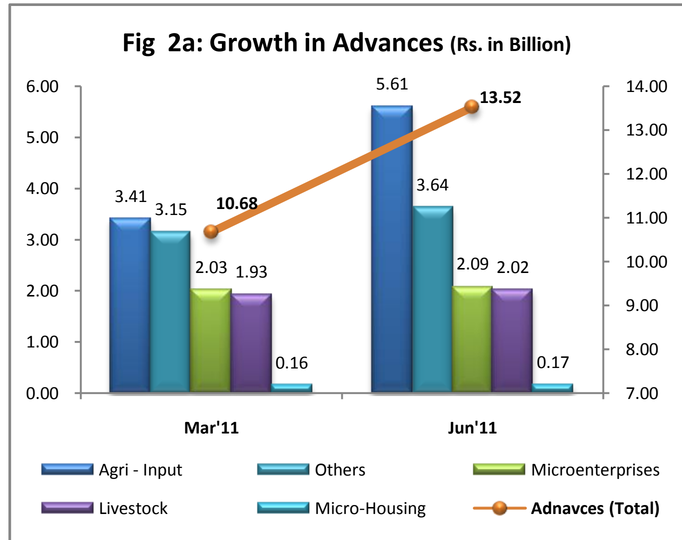
Major developments on funding side were also observed as total funding accelerated from Rs. 20.6 billion to Rs. 26.5 billion during the quarter. All national level MFBs showed significant growth in deposits. In area of borrowing major contribution was seen at NRSP which availed loan facility of Rs. 2.8 billion.

More encouragingly, SBP has recently received concrete interest of strong private sector in existing and new MFBs. This along with quarterly performance generates optimism for microfinance banks to accelerate their growth trajectory in next quarters. Thus, the outlook is positive and the potential of microfinance in Pakistan remains considerable.

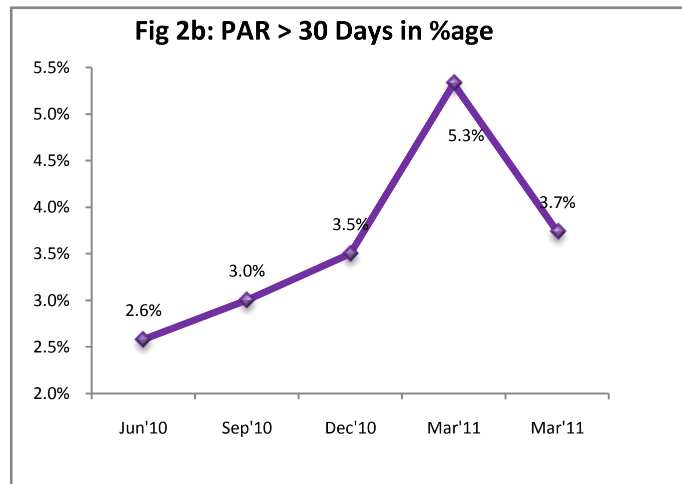
2.1. Advances – Growth, Up-Scaling and Quality

Advances exhibited remarkable growth of 27.0% during the quarter (Figure 2a). This growth was led by all national level MFBs. NRSP MFB transformed its cotton crop loan portfolio of Rs. 2.1 billion and became the 2nd largest player in agricultural financing among other MFBs. Other big players i.e. KBL and FMFBL also disbursed loans for sugar-cane & cotton crops, and livestock during the quarter under review. Additionally, Tameer and

PakOman MFBs also showed notable growth in agri. financing, though they had still shared relatively a small portion of overall agri. loans portfolio.



In microenterprise category, Kashf MFB was leading the growth followed by FMFBL and PakOman. Tameer continued its gold backed financing and caused growth in 'others'[1] category. FMFBL and Tameer also showed growth in housing finance, though this category was still in its infancy stage and shared the smallest portion of the overall microfinance loan portfolio. The inclusion of NRSP's portfolio and growth seen by all categories changes the overall portfolio mix which at present include agriculture (41.5%, Q_1:32%), livestock (15.0%, Q_1:18.0%), microenterprises (15.4%, Q_1:19.0%), housing (1.2%, Q_1:2.0%), and others (27.0%, Q_1:30.0%).



The average outstanding loan size of MFBs is persistently improving and currently stood at Rs.18,952 which indicates that MFBs are gradually up-scaling.

On portfolio quality side, NPLs sharply reduced by 11.0% during the quarter. The big MFBs (particularly FMFBL) controlled their NPLs during the quarter and successfully recovered or rescheduled 70.0% to 75.0% of their flood hit portfolios. Moreover, Pak-Oman finally succeeded in reducing its NPLs during the quarter but still placed at higher node with more than 5.0% NPLs. All these improvements in portfolio quality, together with the growing GLP base on account of NRSP portfolio, dramatically reduced the PAR > 30 days in %age, however, still higher as compare to the previous trends till Dec-10 (**Figure 2b**).

2.2. Alternate Delivery Channels (ADCs)

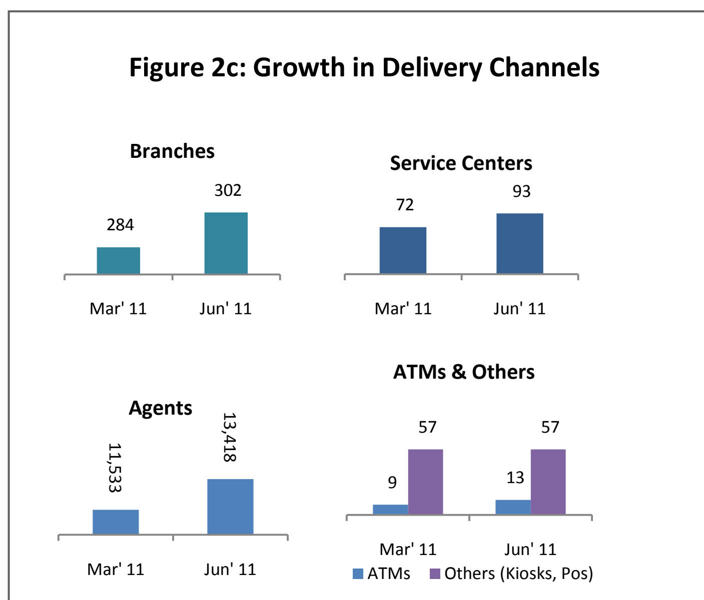
MFBs are forerunner in expanding wide-range of alternative delivery channels, thus radically changing the retail landscape of financial service industry. Moreover, the number of branches has also increased to 302 with the addition of 19 branches of NRSP. The MFBs are increasingly aiming to accelerate the flow of financial services through the use of service centers, branchless banking (BB) agents, kiosks at third party locations, and ATMs (Figure 2c).

---

[1] Others category mainly includes gold based secured financing

This shift from bricks and mortar branches to branchless banking enabled MFBs and their customers to interact remotely in a trusted way through existing local BB retail outlets.

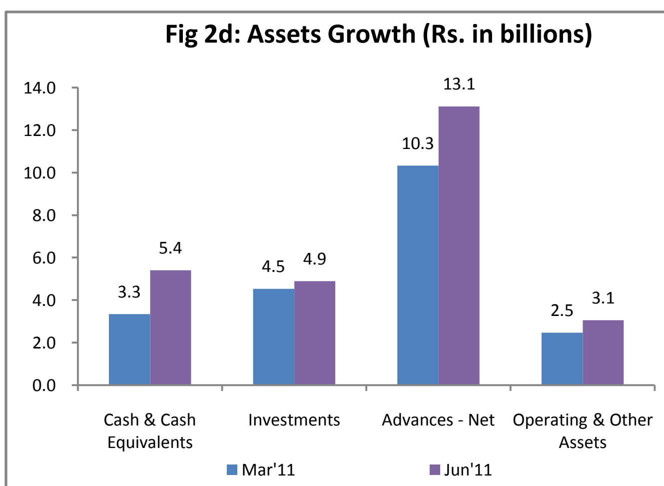
Through mobile account customers can now send & receive money, and pay their utility bills right from their mobile phone, anywhere, anytime. Moreover, they can also avail these services along with deposit and withdrawal of money from any retail BB agent (like easypaisa BB agents of Tameer MFB)



2.3. Assets Growth

The asset-base of MFBs gradually improved over time except a downfall in the previous quarter due to cut in operations by big MFBs in war & flood affected areas. During the current quarter, all the four categories of assets, except investment, showed remarkable growth (Figure 2d) mainly due to the inclusion of NRSP MFB's assets.

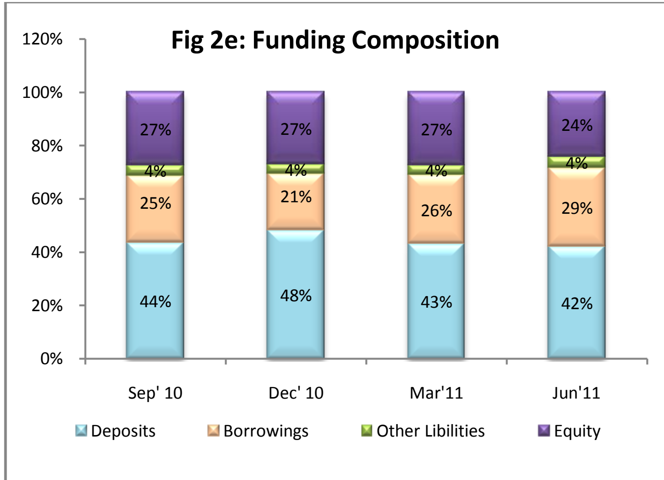
Cash & cash equivalent enhanced by 62.0% mainly because of the grant received by FMFBL and Rs. 1.5 billion excess funding retained by NRSP for fresh lending. The big MFBs (KBL, FMFBL, and Tameer) have increased their investments during the quarter that reasoned for 7.8% growth in investment category. Operating and other assets category has also stipulated growth of about 24.0% during 2nd Quarter 2011.

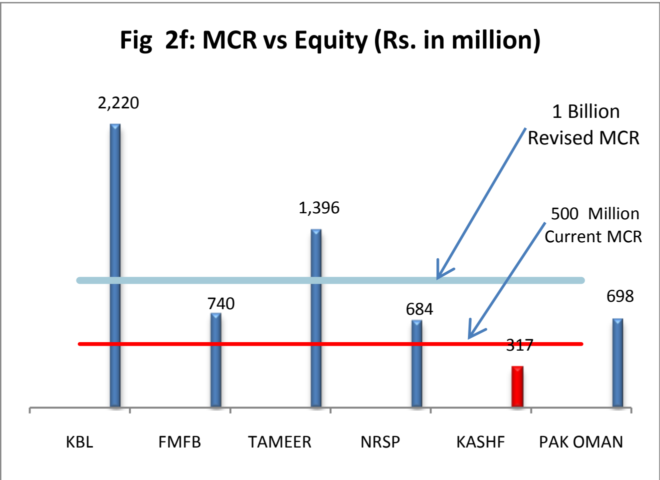


All the above developments has slightly changed the asset mix which at present include Cash & Cash Equivalent (20.0%, Q_1:16.0%), Investments (19.0%, Q_1: 22.0%), Advances – Net (50.0%, Q_1:50.0%) and Operating & Other Assets (12.0%, $Q_1$12.0%).

2.4. Funding Structure

Deposit-Debt mix changed from 43%-26% to 42%-29% in this quarter (Figure 2e). Borrowings increased on account of Rs. 2.8 billion loan obtained by NRSP MFB from NRSP foundation based on the funding line attained from PPAF. Deposits increased by 25.5% with balanced growth in current, savings, and fixed accounts. Tameer MFB has successfully launched its easypaisa mobile accounts thereby dramatically increased the no. of depositors by 73.0% during the quarter, however, the FMFBL still lead in terms of deposits. KBL and FMFBL also showed significant improvement in deposits during the quarter.





On equity side, Kashf MFB is still lacking capital to meet the Minimum Capital Requirement (MCR). The equity of KBL and Tameer MFBs has slightly increased on account of profit declared during the quarter. FMFBL received Rs.148.8 million grant on account of Malakand Relief Package which eventually caused growth in equity.

Figure 2f presents current scenario of MFBs (only national level MFBs including NRSP) including equity position with respect to current and revised MCR.

3.0. Agricultural Finance

3.1. Introduction

The Agricultural Credit Advisory Committee (ACAC) had set an agricultural credit target of Rs. 270 billion for 2010-11. The target was 8.8 percent higher than the disbursement of Rs. 248 billion in 2009-10. Out of the total target, Rs 181.3 billion were allocated to commercial banks, Rs. 81.8 billion to ZTBL and Rs. 6.9 billion to Punjab Provincial Cooperative Bank Limited.

3.2. Agricultural Credit Disbursement

During July 2010-June 2011 banks disbursed an amount of Rs. 263 billion or 97.4% of the annual target of Rs. 270 billion compared with disbursement of Rs. 248 billion or 95.4% of the target of Rs. 260 billion during corresponding period last year. Annual growth remained modest with a rise of Rs. 14.9 billion or around 6.1% compared with corresponding period last year.

Quarter wise disbursement reveals that banks disbursed Rs. 94.3 billion during Apr-Jun-11 compared with disbursement of Rs. 67.1 billion in Jan-Mar-11 (preceding quarter) and Rs. 81.8 billion in the same quarter last year. Detail of indicative agricultural credit targets of Rs. 270 billion for FY11 and actual disbursements by banks up to Jun-11 and in the corresponding period last year are given in Table 3A.

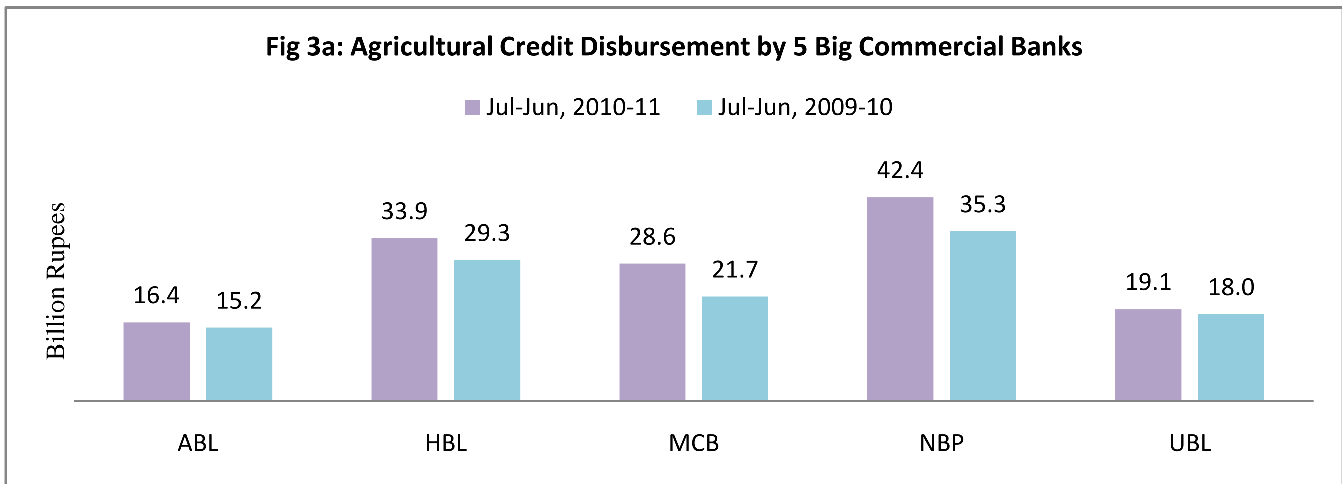
Table 3A: Indicative Agri. Credit Targets and Disbursement

(Billion Rupees)

Banks	Target 2010-11	Disbursement 2010-11			Target 2009-10	Disbursement 2009-10		
		Jan-Mar 2011	Apr-Jun 2011	Jul-Jun 2010-11		Jan- Mar 2010	Apr-Jun 2010	Jul-Jun 2009-10
5 Big Banks	132.4	38.2	47.0	140.2	124.0	29.7	34.4	119.6
ZTBL	81.8	16.4	28.0	65.4	80.0	18.6	30.0	79.0
DPBs	48.9	11.0	16.5	50.2	50.0	10.4	15.1	43.8
PPCBL	6.9	1.5	2.8	7.2	6.0	1.2	2.2	5.7
Total	**270.0**	**67.1**	**94.3**	**263.0**	**260.0**	**60.0**	**81.8**	**248.1**

Bank-wise break up of agri. credit disbursement reveals that during July-June 2010-11 five major banks as a group disbursed Rs. 140.2 billion or 105.9% of the whole year targets, ZTBL disbursed Rs. 65.4 billion or 79.9% of the targets, Domestic Private Banks (DPBs) disbursed Rs. 50.2 billion or 102.6% of the targets and PPCBL disbursed Rs. 7.2 billion or 104.6% of the targets. While performance of 5 major commercial banks, PPCBL and DPBs showed some improvement compared with last year's disbursements, the performance of ZTBL remained slow, which is the reason the whole year's target could not be achieved.

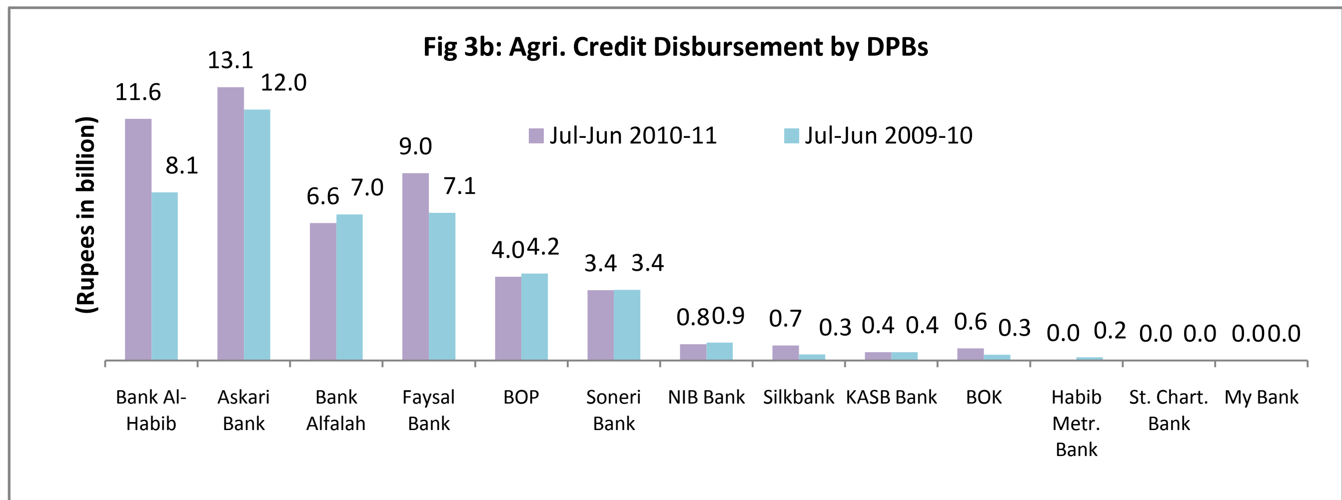
During Apr-Jun-11 five major banks as a group disbursed Rs. 47 billion or 35.5% of their whole year targets, ZTBL disbursed Rs. 28 billion or 34.2% of target, Domestic Private Banks (DPBs) disbursed Rs. 16.5 billion or 33.8% of target and PPCBL disbursed Rs. 2.8 billion or 40.1% of target. The cumulative position of agri. credit



disbursements by five major banks for the period July-June, 2010-11 and, 2009-10 has been illustrated in figure 3a.

Comparative analysis/ position of agri. credit disbursement by DPBS during July-June, 2009-10 and July-June, 2010-11 is illustrated in figure 3b.

Sector-wise classification indicates that out of Rs. 263 billion disbursement during Jul-Jun-11 an amount of Rs.

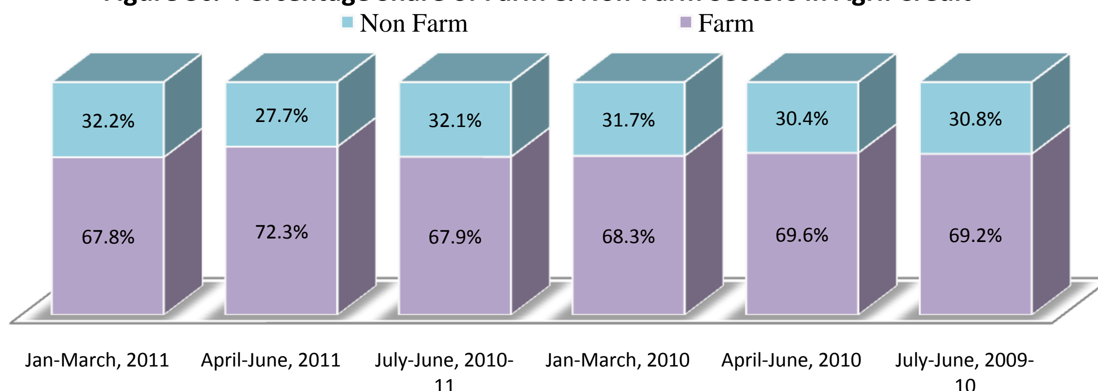


178.7 billion was disbursed in farm- sector and Rs. 84.3 billion were extended to non-farm sector. Last year during the same period an amount of Rs. 171.8 billion was extended to farm sector and Rs. 76.4 billion was disbursed to non-farm sector. The share of non-farm sector has increased from 30.8% to 32.1% YoY. There has been a continuous rising trend in the share of non-farm sector over the last few years mainly due to SBP's initiatives, i.e. issuance of guidelines for non- farm sector in the areas of livestock, fisheries and poultry financing, rising domestic demand for fish & poultry, increase in export of livestock, etc. Quarter-wise

disbursement to farm and non-farm sectors is given in Table 3B, while their percentage share in agricultural credit disbursement is given in Figure 3c.

Table 3B: Credit Disbursements to Farm & Non-Farm Sectors (Rs. Billion)							
	Sector	2010-11			2009-10		
		Jan-Mar 2011	Apr-Jun 2011	Jul-Jun 2010-11	Jan-Mar 2010	Apr-Jun 2010	Jul-Jun 2009-10
A	**Farm Credit**	**45.5**	**68.2**	**178.69**	**41.0**	**56.9**	**171.76**
1	Subsistence Holding	27.9	36.3	102.22	24.0	34.4	103.32
i	*Production*	27.0	35.3	98.47	21.2	32.0	92.62
ii	*Development*	0.8	0.9	3.75	2.8	2.5	10.70
2	Economic Holding	11.8	21.9	50.55	10.9	16.1	44.97
i	*Production*	11.5	21.6	49.50	10.3	15.4	42.26
ii	*Development*	0.2	0.3	1.05	0.6	0.7	2.71
3	Above Economic Holding	5.8	10.1	25.92	6.1	6.4	23.47
i	*Production*	5.7	9.4	24.50	5.9	6.2	22.22
ii	*Development*	0.1	0.7	1.42	0.3	0.3	1.25
B	**Non-farm Credit**	**21.6**	**26.1**	**84.33**	**19.0**	**24.9**	**76.38**
1	Small Farms	4.9	8.1	20.80	4.0	6.4	17.46
2	Large Farms	16.8	18.0	63.54	15.0	18.5	58.92
	Total (A+B)	**67.1**	**94.3**	**263.02**	**60.0**	**81.8**	**248.14**

Figure 3c: Percentage Share of Farm & Non-Farm Sectors in Agri. Credit



3.3. Province-wise Disbursement

Province wise agri. credit disbursement position during Jul- Jun-11 shows that out of total disbursement of Rs. 263 billion, Rs. 224.5 billion or 85.3% were disbursed in Punjab, Rs. 30.5 billion or 11.6% in Sindh, Rs. 7 billion or

2.7% in Khyber Pakhtunkhwa (KPK), Rs. 0.3 billion or 0.1% in Baluchistan, Rs. 0.54 billion or 0.2% in AJK and 0.24 billion or 0.1% in Gilgit-Baltistan (GB).

During April-June, 2011 quarter, Rs. 77.5 billion were disbursed in Punjab which is 36.8% of the annual target, Rs. 14.3 billion in Sindh or 37.8% of the target, Rs. 2.3 billion in Khyber Pakhtunkhwa or 13.9% of the target, 0.1 billion in Baluchistan or 2.3% of the target, and Rs. 0.2 billion in AJK & Gilgit-Baltistan which is 12.5% of the target. Overall Rs. 94.3 billion have been disbursed in all the provinces during the quarter under discussion which is 34.9% of the annual target.

Table 3C: Province-wise Indicative Agri. Credit Targets and Disbursement

(Billion Rupees)

Province	Target 2010-11	Disbursement 2010-11			Target 2009-10	Disbursement 2009-10		
		Jan-Mar 2011	Apr-Jun 2011	Jul-Jun 2010-11		Jan-Mar 2010	Apr-Jun 2010	Jul-Jun 2009-10
Punjab	210.6	57.9	77.5	224.5	202.8	51.4	71.1	213.5
Sindh	37.8	6.7	14.3	30.5	36.4	6.4	8.5	26.7
KPK	16.2	2.2	2.3	7.0	15.6	1.8	1.9	6.5
Baluchistan	4.1	0.1	0.1	0.2	3.9	0.2	0.2	0.6
AJK & GB	1.4	0.2	0.2	0.8	1.3	0.2	0.2	0.8
Total	**270.0**	**67.1**	**94.3**	**263.0**	**260.0**	**60.0**	**81.8**	**248.1**

This analysis reveals considerable improvement in agri. credit disbursement in Punjab (5.1% growth), Sindh (14.1% growth), Khyber Pakhtunkhwa (7.8%), AJK (13.2% growth), whereas, Baluchistan and Gilgit-Baltistan continued the declining trend in agri. credit disbursement of last year. The share of other provinces and regions apart from Punjab is negligible in agri. credit due to weak demand, deteriorating law and order situation, documentation issues and shyness of banks to expand their agri. credit exposure. Details of province-wise disbursements, vis-à-vis targets achieved are given in Table 3C.

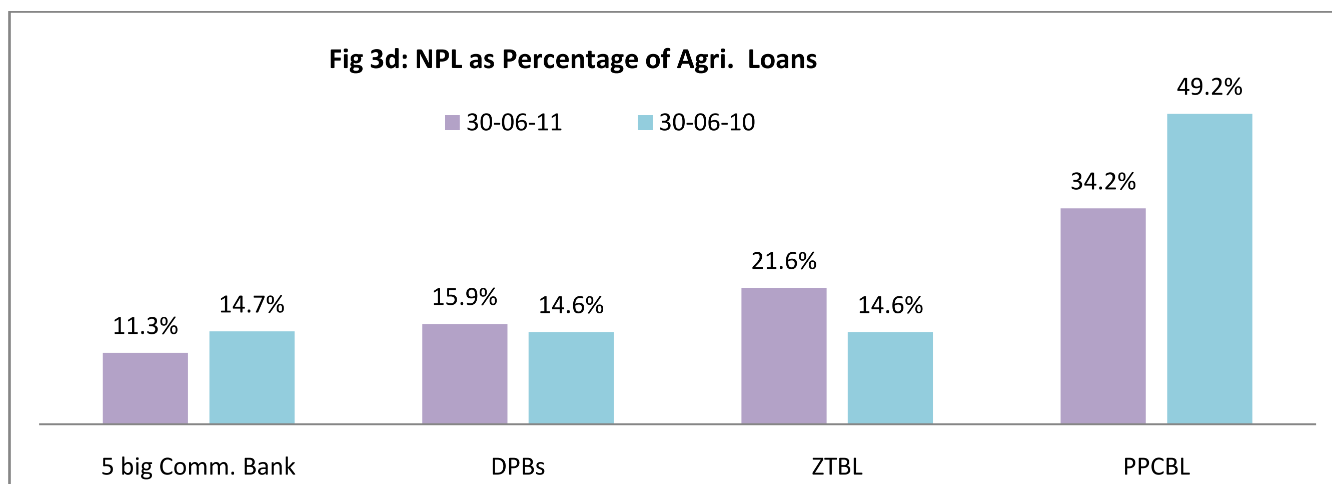
Table 3D: Agri. Non-Performing Loans (Rs. Billions)

Banks	30-06-11 NPLs	30-06-11 Outstanding loans	30-06-10 NPLs	30-06-10 Outstanding loans
5 big Banks	6.86	60.70	7.65	51.96
DPBs	3.72	23.35	3.39	23.18
ZTBL	19.40	89.62	13.13	90.07
PPCBL	2.38	6.95	3.33	6.78
Total	**32.35**	**180.62**	**27.50**	**171.99**

3.4. Agri. Non-Performing Loans

Non-performing loans in agri. financing stood at Rs. 32.35 billion or 17.9% of the outstanding loans as on 30th June, 2011 compared with Rs. 27.5 billion or 16% of the outstanding loans as on 30th June, 2010. Bank wise detail of NPLs is given in Table 3D.

Figure 3d shows NPLs' position of banks as a percentage of their outstanding loans as on end June 2010 and 2011.



3.5. Number of Agri. Loan Borrowers

The number of agri. loan borrowers was 1.779 million as on 30th June, 2011 against 1.81 million as on 30th June, 2010 showing an attrition of around 1.26%. Bank-wise position of outstanding number of borrowers reveals that decrease in number of borrowers was witnessed especially in ZTBL, DPBs, marginally in 5 major banks, while number of borrowers of PPCBL showed a modest improvement. High mark up rate, increasing NPLs and defaults in repayment due to a variety of reasons like recent floods, law & order situation, good prices of wheat and cotton in non-flood affected areas improving cash flow of farmers resulted in decline in outstanding number of borrowers over the period. Shown in Table 3E

Table 3E: Outstanding Number of Agri. Loan Borrowers

Banks	As on 30-06-2011		As on 30-06-2010	
	No. of Borrowers	%Share	No. of Borrowers	Share
5 Big Banks	423,418	24	425,400	23
ZTBL	1,135,293	63	1,147,396	63
DPBs	36,336	2	55,032	3
PPCBL	195,325	11	185,321	10
Total	**1,790,372**	**100**	**1,813,149**	**100**

4.0. Housing Finance

In Pakistan, rapid urbanization has become a challenge for increasing number of people. Studies indicate that lack of finance from a formal source is primarily a supply-side problem. Most of the housing finance is arranged through personal resources. The formal financial sector caters to only 1 to 2 percent of all housing transactions in the country, whereas the informal lending caters up to 10-12% of such transactions. Presently, the formal financial sector provides housing support through two major sources namely the Government owned House Building Finance Corporation (HBFC) and private commercial banks.

The property development industry suffers from low public confidence. Financial weaknesses and the absence of clear, uniform and fair business practices have affected its credibility contributing to the reluctance of financial institutions in providing development and construction finance. There is a strong need to strengthen the property titling and land administrative procedures including improvements of the legal provisions, standardization of processes, and computerization of all relevant revenue records. These steps will enhance the financing by the formal sector. Weakness in the existing legal framework also impedes the financing opportunities of the formal financial sector. Though the Financial Institution Recovery Ordinance, 2001 empowers the financial institutions in case of default to foreclose a mortgage property without recourse to the court of law, lack of full implementation of the recovery law in its letter and spirit dilutes its effectiveness in protection of rights of the respective parties, i.e., the financial institutions, mortgagors, landlords and tenants, thus needing a major improvement.

Although the regulatory framework for land registration and transfer regime exists in Pakistan, the process by which land is acquired and registered is cumbersome at times, because of number of institutions and registration procedures required to execute property transactions. Land records are manually maintained leading to errors and omissions and resultantly they have modest commercial value for the mortgagee financial institutions especially in rural and some urban areas. The lack of efficient and reliable system of ascertaining the bona-fide of property titles has forced banks to limit the access of housing finance to a certain number of urban localities within the urban centers.

National and local master plans for town planning and housing facilities are either inadequate or poorly enforced, which lead to inefficient allocation of land and uncontrolled urban development. Lack of transparency and accountability in the planning process also give opportunities to land grabbers/mafias to have valuable inside information as to future infrastructure developments or to be able to influence such plans so that value of its land increases. Over-restrictive building codes and laws on subdivision limit the efficient use of urban land and increase the price to consumers, especially in zones having relatively higher prices of lands in high land price zones. Moreover, the large scale projects often get delayed due to failure of utility companies in connecting new housing developments in time.

The “property valuers” have professional conduct requirements that were established by SBP and the Pakistan Banks’ Association (PBA), whereas majority of real estate builders and developers are working as sole proprietorships or partnerships with limited capital and informal corporate governance structures. Absence of sound governance structure within the housing developer industry creates lack of good practices, illegal construction, unreliable building permits, and legally unprotected advance purchase of units that are required to be built in future. The unstructured and unsupervised nature of business of real estate brokers/ agencies, which could serve as natural arrangers for the provision of financial services, is also a significant constraint to the

provision of housing and housing finance. Consequently, it is difficult for financial institutions to verify the character, capital, and capacity of potential clients. Risk assessment and portfolio valuation is also fragile, which is another factor for the lenders' extreme caution for transaction initiated by these venture. As a result, financial institutions are reluctant to enter this market, which in turn causes scarcity of finance and constraints in the supply of housing. In the absence of the formal arrangements between the housing developers/real estate agents etc and financial institutions, the protection of individual purchasers remains limited as the market is dominated by cash transactions with limited availability of systematic information in a transparent manner. Without using a strong regulatory authority to enforce corporate governance and allied standards for this stratum of business entrepreneurship, the quality of availability of housing facilities across population spectrum will not improve.

At present, 27 commercial banks, House Building Finance Corporation (HBFC), one DFI and two microfinance banks are catering to housing finance needs. HBFC is the only specialized housing bank in the country, which has been providing housing finance to public since 1952. Commercial banks entered the mortgage business during 2003 contributing very small share in the housing finance system. Although HBFC's share in the total housing finance has reduced in absolute terms, it is still the only institution that continues to cater to the lower-middle and low-income groups and enjoys the largest customer base. Recently microfinance banks have also started serving the lower-middle income groups.

After demonstrating a promising growth trend till 2008, the housing finance sector has recently been showing a declining trend. The total outstanding reported by banks and DFIs as on Jun-11 was Rs. 61.9 billion as compared to Rs. 70.3 billion as on June 30, 2010 (a decline of 12.0**%**) and Rs. 65.4 billion at the end of Mar-11. The total number of outstanding borrowers has also decreased from 101,632 to 95,553 since Jun-10; showing a fall of 5.98%.

Approximately 898 new borrowers were extended house finance during the quarter (Apr-Jun-11), accounting for Rs. 1.5 billion of new disbursements. HBFC accounted for 56.7% of these new borrowers and contributed 22.4% of the new disbursements equivalent to Rs. 337 million.

Financing for outright purchase continued to dominate financing for construction and renovation by comprising almost 57.0% share in gross outstanding portfolio. Outstanding portfolio for construction and renovation was 34.0% and 9.0**%** respectively.

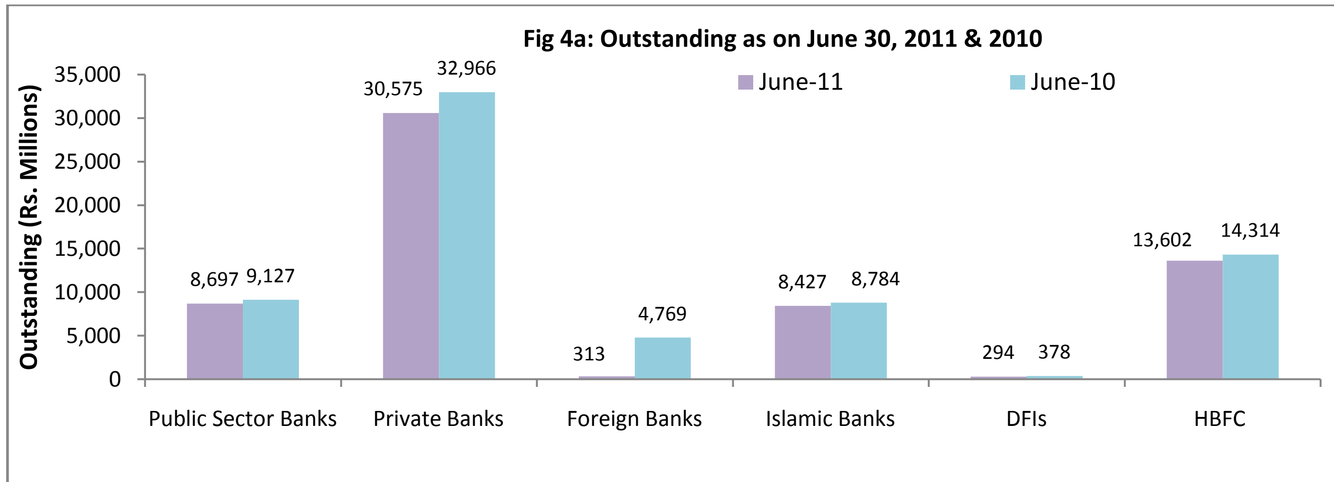
Non-performing loans have increased from Rs. 17.4 billion (Jun-10) to Rs. 18.7 billion (Jun-11); a 7.6% increase over the year. The stock of NPLs as on Mar-11 was Rs. 18.9 billion. However; this rise in NPLs is not unique to housing finance and is only depicting the overall increase in NPLs of all sectors witnessed in the banking industry during the past year.

4.1. Gross Outstanding

The total outstanding finance as on Jun-11 of all banks and DFIs stood at Rs. 61.9 billion, as compared to Rs. 65.4 billion as on Mar-11, showing a decrease of Rs. 3.5 billion (5.4%). Compared to quarter under review, outstanding of all commercial banks and DFIs collectively decreased by 12.0%.

Banking sector-wise total outstanding on quarters ending Jun-10 & 11 are shown in Figure 4a. Of the total outstanding as on Jun-11, commercial banks accounted for Rs. 48.0 billion; a 13.7% decline since quarter ending Jun-10. Private banks reported Rs. 30.6 billion followed by Islamic banks of Rs. 8.4 billion, public sector banks of

Rs. 8.7 billion and foreign banks with Rs. 0.32 billion. The outstanding loans of HBFC were Rs. 13.0 billion; down by 5.0% over the last year. Other DFIs have a meager share of Rs. 0.29 billion in outstanding loans.



The total outstanding housing finance as on Jun-11 of Islamic Banking Industry (05 Islamic Banks & 13 Islamic Banking Divisions of Conventional Banks) stood at Rs. 12.5 billion. Compared to quarter ending Mar-11 (Rs. 14.0 billion), outstanding of Islamic banking Industry decreased by 10.5**%.**

Of the total outstanding Islamic housing finance, Islamic banks accounted for Rs. 8.4 billion (a 12.9% decrease over the last quarter Mar-11) and IBDs of conventional banks posted Rs. 4.1 billion (a 5.2% decline since quarter ending Mar-11).

4.2. Non-Performing Loans

NPLs have increased from Rs. 17.4 billion (Jun-11) to Rs. 18.0 billion (Jun-11); a 7.6% increase during the year. The stock of NPLs as on Mar-11 was Rs. 18.9 billion, showing a decrease of 1.2 % during a quarter (Apr-Jun-11). Figure 4b shows a comparison of existing NPLs status of different banking sectors with last year.

Figure 4c compares NPLs as a percentage of outstanding portfolio at the end of quarters on Jun-11 and Jun-10. NPLs as a proportion of total outstanding have witnessed an increasing trend over the last twelve months. This overall rise in NPLs is primarily due to rising inflation and high interest rates.

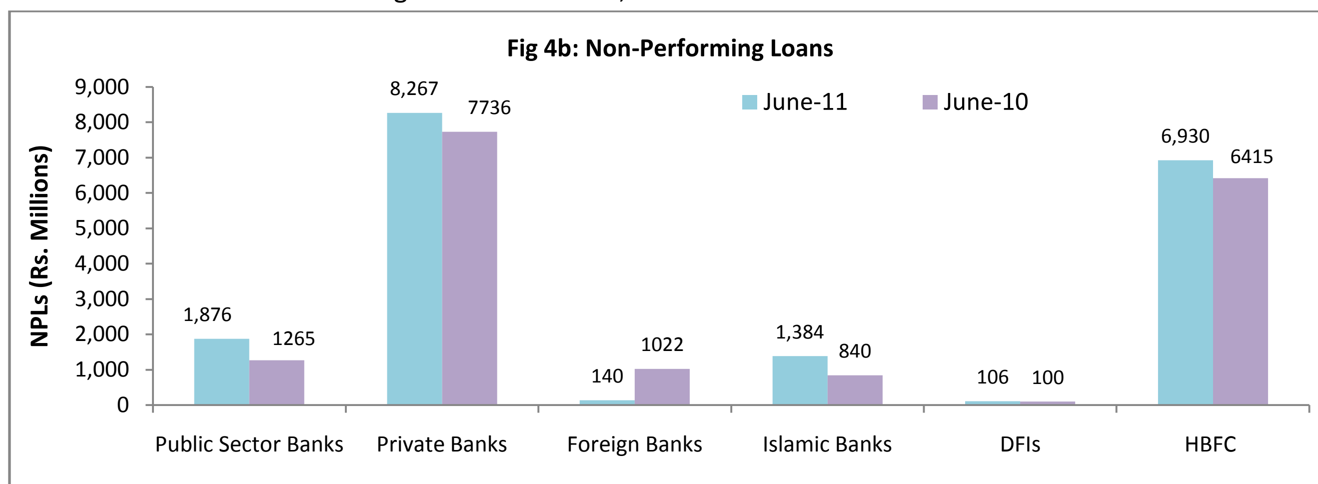
HBFC's NPLs have increased from Rs. 6.4 billion to Rs. 6.9 billion during the year; an 8.0% increase.

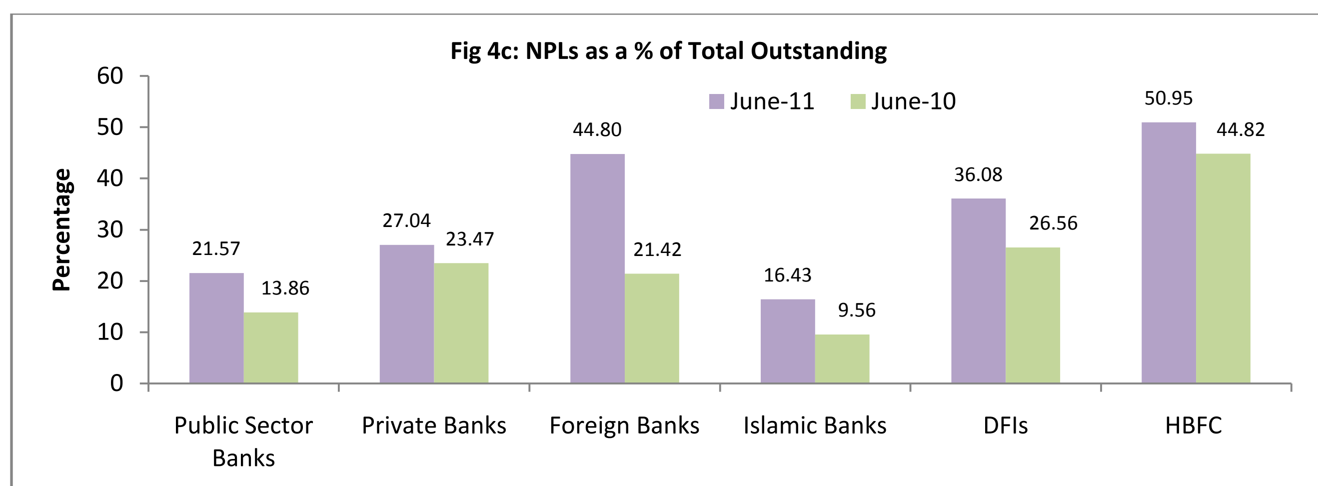
Although growth of its NPLs remains relatively low in absolute terms when compared to some of the other banking sectors, its percentage share in its total outstanding, however, is the greatest, as 51.0% of its total outstanding constitutes NPLs (Figure 4c). HBFC's percentage share in total NPLs is 37.1%.

Excluding HBFC, NPLs for all banks and other DFIs have increased by 7.4% over the year from Rs. 6.4 billion to Rs. 6.9 billion. The percentage share of NPLs that all banks and other DFIs (excluding HBFC) constitute is 24.4% of their total outstanding portfolio, compared to a 19.6% as on Jun-10.

Among banks, non-performing finances (NPFs) of Islamic banks witnessed the sharpest increase of almost 64.8% during the year, from Rs. 840 million to Rs. 1.4 billion. Their NPFs constitute 16.4% of total outstanding, which was only 9.6% on Jun-10. NPLs of the public sector banks have increased from Rs. 1.3 billion to Rs. 1.9 billion (an increase of 48.3%) which are 21.6% of their total outstanding. Private banks' NPLs have increased by 6.9%, from Rs. 7.7 billion to Rs. 8.3 billion which is 27.0% of their total outstanding as against 23.5% on Jun-10.

NPLs of foreign banks as a percentage of their outstanding portfolio increased from 21.4% at the end of last year to 44.8. NPLs of DFIs (excluding HBFC) have increased from Rs. 100 million to Rs. 106 million, a 5.5% increase with 36.1% of its total outstanding classified as NPLs, which was 26.6% on Jun-10.





Non-Performing Finances (NPFs) for Islamic Banking Industry (IBs & IBDs) were reported 2.2 billion on Jun-11 which were Rs. 2.3 billion at the end of last quarter (Jan-Mar-11) showing decrease of 3.6%.

4.3. Number of Borrowers

Total number of outstanding borrowers has decreased from 101,632 to 95,553 since Jun-10; a decline of 6.0%. As shown in Figure 4d, there is a decrease in no. of borrowers in each category except Islamic banks and private banks, where numbers increased from 2,240 to 2,895 and 12582 to 14,154 respectively.

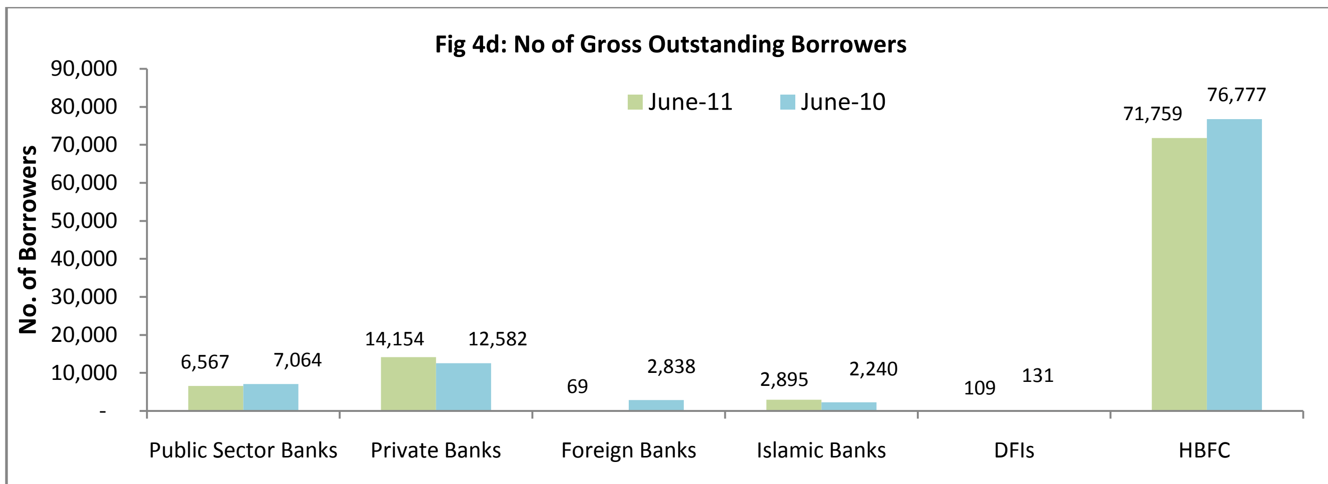
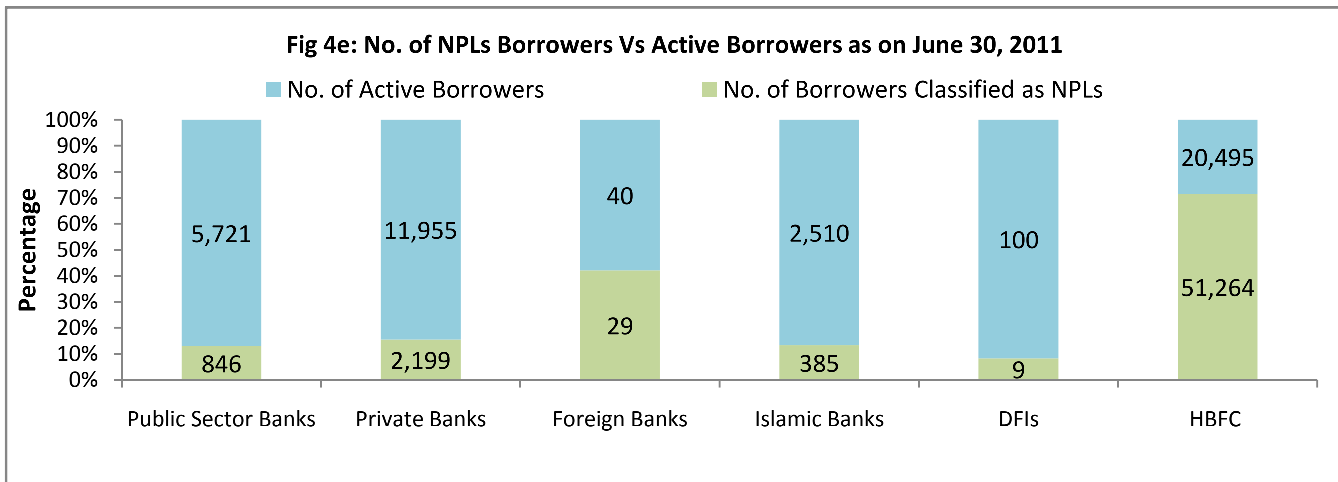


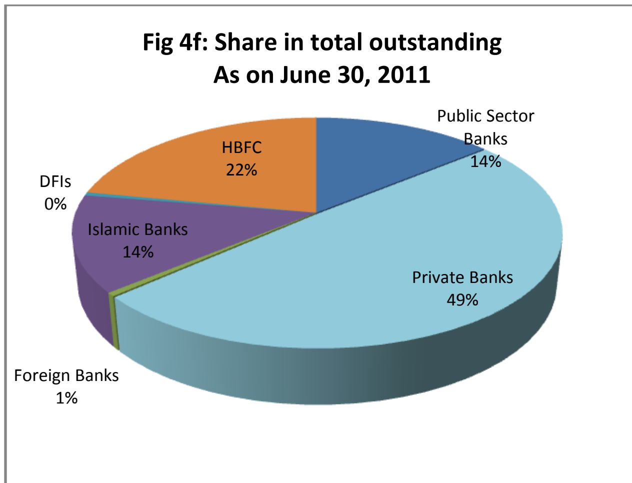
Figure 4e shows number of borrowers that has been classified as NPLs as a percentage of total borrowers. In terms of numbers, approximately 57.3% of total borrowers of housing finance borrowers have been classified as non-performing. However, this is primarily due to HBFC's number (51,264) of non-active borrowers, classified as non-performing, which comes to 71.4% of its total borrowers. Thus, excluding HBFC in such an analysis will be important as it caters to 78.0% of the total borrowers in housing finance sector which accounts for only 22.0% of

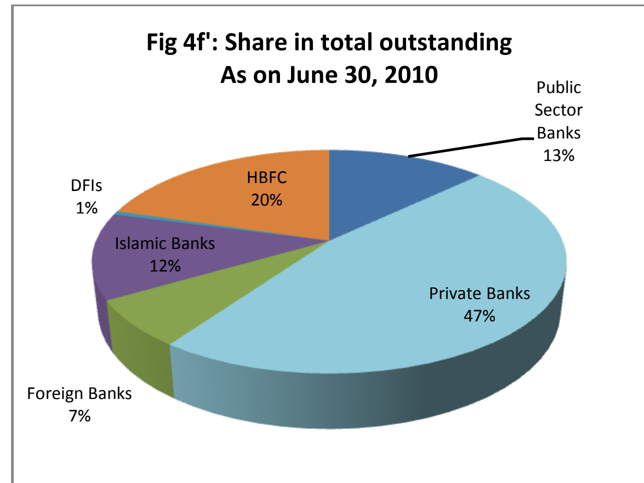


total outstanding portfolio. Thus, by excluding HBFC, 15.0% of total borrowers of housing loans have been classified as non-performing. Total number of customers served by Islamic Banking Industry increased from to 4,065 to 4,089 (an increase of 0.59%) since Mar-11.

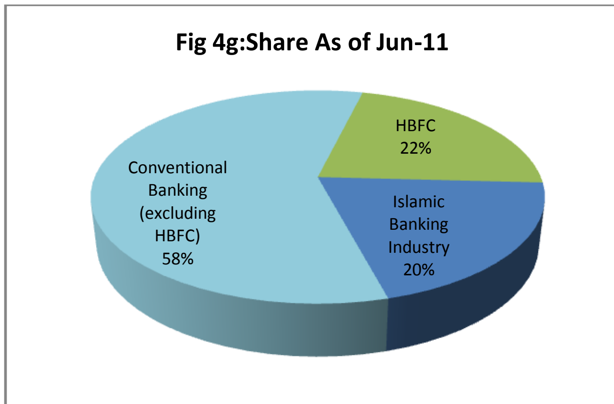
4.4. Share of Banks

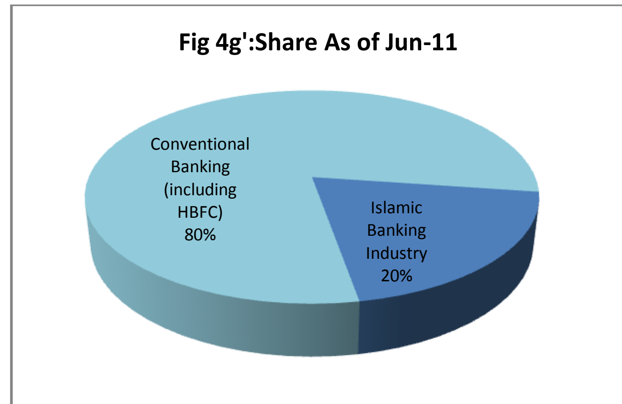
The overall market share (based on gross outstanding) of commercial banks (excluding DFIs) remained the same since the end of last year, as 78.0%. In comparison with last quarter (Mar-11), there was 79.0%. Within commercial banks, the share of private banks in the total outstanding increased marginally from 47.0% to 49.0% and the share of foreign banks decreased from 7.0% to 1.0% due to take over of RBS portfolio by Faysal Bank (Figure 4f &4f'). The share of public sector banks and Islamic Banks in the total outstanding increased from 13.0% to 14.0% and 12.0% to 14.0%. Share of HBFC in the total outstanding increased from 20.0% to 22.0% since the end of last year.

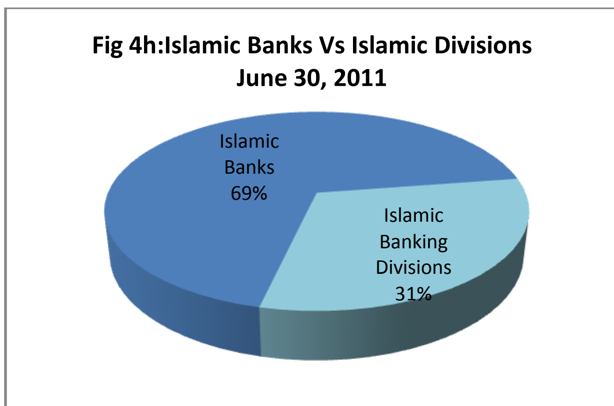


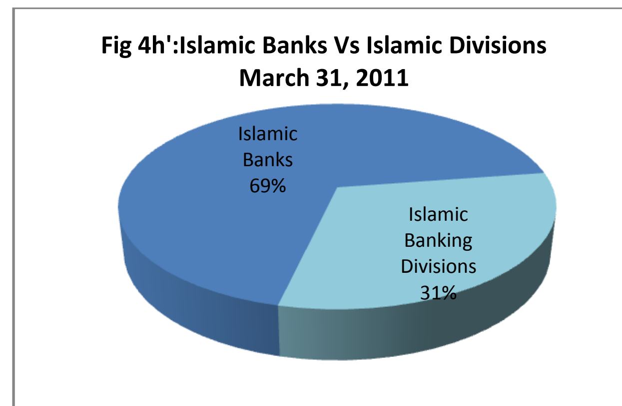


The share of Conventional Banking (excluding HBFC), Islamic Banking Industry and HBFC in the total outstanding was 58%, 20% and 22% respectively on Jun-11. IBDs (13 windows) and Islamic banks (05 banks) have 69% and 31% share in housing finance portfolio of Islamic Banking Industry (Figure 4g & 4g'), which shows that conventional banks also consider the Islamic mode of financing an important part of their business strategy. One of the reasons of increasing Islamic banks outstanding portfolio is the purchase of Citibank's portfolio of Rs. 888 million by BankIslami in the quarter ending Dec-10.









4.5. Disbursements

Fresh disbursements to the tune of Rs. 1.5 billion were made to 898 borrowers during the quarter ending Jun-11 (Table 4A).

Private banks extended new disbursements with Rs. 637 million followed by Islamic banks with Rs. 449 million public sector banks with Rs. 48 million and foreign banks with Rs. 0.31 million.

HBFC's fresh disbursements for the quarter were reported to be Rs. 337 million. Among commercial banks, the number of new borrowers totaled 389, with private banks serving 221 borrowers and Islamic banks 136 borrowers. HBFC extended loans to 509 new borrowers during the reporting quarter.

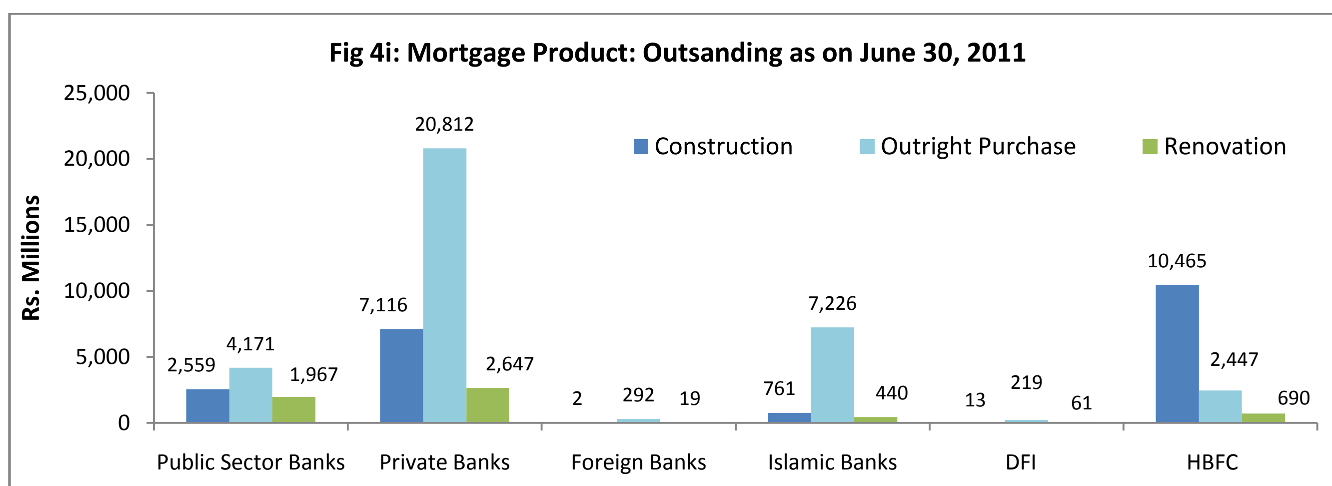
Table 4A: New Disbursements during the quarter		
	Amount (Rs. Millions)	No. of Borrowers
Public Banks	48	25
Private Banks	637	221
Foreign Banks	31	7
Islamic Banks	449	136
All Banks	**1165**	**389**
DFIs	-	-
HBFC	337	509
Total	**1,502**	**898**
Islamic Industry	586	174

Fresh disbursement for Islamic Banking Industry was Rs. 586 million to 174 new borrowers during the quarter ending June 30, 2011 (Table 4A). This includes new disbursements of Rs. 137 million to 38 customers by IBDs of conventional banks.

4.6. Sectoral Share

The biggest share of housing finance continued to be attracted towards outright purchase (Figure 4i). The outstanding for outright purchase stood at Rs. 35.2 billion as on Jun-11; a 57.0% share in total outstanding of Rs. 61.9 billion. This is followed by the construction category where outstanding reported at quarter-end stood at Rs. 20.9 billion and that of renovation stood at Rs. 5.8 billion.

Active portfolio shows that private banks have taken a lead in financing for all three sectors; construction 34%, outright purchase 59% and renovation 45%.



4.7. Housing Finance Business of Micro Finance Banks

Gross Outstanding

The total outstanding housing finance as on Jun-11 of Micro Finance Banks (MFBs) stood at Rs. 169.6 millions, which was Rs. 161.6 millions at the end of Mar-11, showing an increase of 5.0%, over the last quarter.

Number of Borrowers

Total number of outstanding borrowers has increased from 2,222 to 2,297 since Mar-11; an increase of 3.4%.

Non-Performing Loans

NPLs for Micro Finance Banks have increased from Rs. 1.25 million (Mar-11) to Rs. 1.6 million (Jun-11); a 25.6% increase over the last quarter. NPLs of MFBs arising out of housing finance business are around 1.0% of their outstanding housing finance portfolio.

4.8. Analysis of Loan Variables adopted by Banks/DFIs & HBFC

Tables 4B, 4C & 4D summarize loan variables across all banking sectors including weighted average interest rate, Loan-to-Value ratio (% financing by banks), average maturity period, average loan size and average time for loan processing.

Weighted average interest rate

The overall weighted average interest rate was 17.3% at the end of the current quarter. Highest weighted average profit rate was reported by HBFC 17.5%, followed by public sector banks 17.2%, private banks 17.1%, and Islamic banks 17.0% while foreign banks average came to 15.6%.

Average maturity periods

Average maturity period of outstanding loans as on Jun-11 came to 12.5 years, which is low as compared to quarter ending Jun-10 when it was 13 years. HBFC's average maturity period is reported to be 12.5 years, while that of Islamic banks is 10.7 years. Table 4A shows that among commercial banks, foreign sector banks have extended housing loans for an average tenure of 17.5 years followed by private sector banks with 13.2 years and public sector banks with 10.1 years

Loan to Value ratio

The percentage of financing (Loan to Value ratio) extended by banks and DFIs increased during last year (Table 4B) from 42.3% to 42.6%. Average LTVs of commercial banks have increased from 42.3% to 42.6%. The average LTV for HBFC has decreased from 57.2% to 42.8% during the last year, which is a significant change.

Average time for loan processing

The reported average time for loan processing is approx. 25.8 days for all banks and DFIs (except HBFC), which was 27.8 days in Jun-10. Average time taken by HBFC presently is 41.7 days. This has increased overall industry

average to 33.7 days. Currently, the application processing of most of the banks is a centralized process, where branches forward applications to central branches/head offices for assessment and approvals.

Average loan size

Average loan size for disbursements made during the quarter ending Jun-11 is Rs. 3.2 million for all banks, except HBFC. The average loan size for HBFC is reported to be Rs. 1.9 million for the reporting quarter. Islamic as well as private banks reported an average finance size of Rs. 1.9 and 4.7 million, foreign banks Rs. 2.5 million and public sector banks reported Rs. 0.8 million. The housing finance market is still inclined towards lending to high income groups.

Table 4B	Weighted Average Interest Rate (%)					Average Maturity Period (Years)				
	June-10	Mar-11	Dec-10	Sep-10	June-10	June-10	Mar-11	Dec-10	Sep-10	June-10
Public Sector	17.2	16.8	15.9	13.8	13.7	10.1	13.2	10.6	9.8	11.3
Private Banks	17.1	17.1	16.4	15.0	15.1	13.2	13.0	11.0	10.0	13.0
Foreign Banks	15.6	14.1	16.1	16.9	16.3	17.5	20.0	14.8	9.5	11.6
Islamic Banks	17.0	17.3	16.6	16.3	16.9	10.7	12.2	10.0	11.4	12.6
All Banks	17.0	16.9	16.3	15.5	15.5	12.3	13.2	11.1	10.4	12.3
DFIs	-	16.8	16.6	16.3	16.2	-	-	-	-	-
All Banks & DFIs	17.0	16.9	16.3	15.6	15.6	12.3	13.2	11.1	10.4	12.3
HBFC	17.5	17.5	17.0	16.2	16.1	12.7	13.5	13.3	12.9	13.6
Total Average	17.3	17.2	16.7	15.8	15.7	12.5	13.4	12.2	11.7	13.0

Table 4C	Loan to Value Ratio					Average Time for Loan Processing (days)				
	June-10	Mar-11	Dec-10	Sep-10	June-10	June-10	Mar-11	Dec-10	Sep-10	June-10
Public Banks	31.7	49.6	62.1	52.4	35.1	38.0	38.4	32.6	16.8	24.6
Private Banks	44.6	49.4	55.0	45.9	39.7	22.6	28.5	21.3	19.7	25.1
Foreign Banks	63.4	65.5	50.1	33.2	54.1	30.0	30.0	25.5	30.0	33.2
Islamic Banks	39.7	42.2	53.2	51.4	32.7	23.2	25.0	28.4	29.1	25.5
All Banks	42.6	48.5	55.2	48.1	42.3	25.8	28.8	26.2	23.3	27.8
DFIs	-	-	-	-	-	-	-	-	-	-
All Banks & DFIs	42.6	48.5	55.2	48.1	42.3	25.8	28.8	26.2	23.3	27.8
HBFC	42.8	44.7	43.5	48.5	57.2	41.7	39.1	40.4	48.3	47.8
Total Average	42.7	46.6	49.3	48.3	49.8	33.7	33.9	33.3	35.8	37.8

Table 4D	Average Loan Size				
	June-10	Mar-11	Dec-10	Sep-10	June-10
Public Banks	0.8	2.5	1.1	1.4	1.3
Private Banks	4.7	4.5	2.9	3.2	4.9
Foreign Banks	2.5	2.4	1.7	2.2	2.1
Islamic Banks	1.9	2.1	2.9	2.6	3.1
All Banks	3.2	3.5	2.5	2.6	3.5
DFIs	-	-	-	-	-
All Banks & DFIs	3.2	3.5	2.5	2.6	3.5
HBFC	1.9	1.2	1.2	1.6	1.2
Total Average/Total	2.5	2.3	1.9	2.1	2.3

Conclusion

The quarter ending Jun-11 depicted a slight decrease as compared to quarter ending Jun-10, in overall portfolio. NPLs of the housing finance portfolio display a decreasing trend and banks continue to show signs of cautious lending amidst decreased affordability of the borrowers. LTVs and maturity periods have decreased over the last year. However, the lack of a conducive institutional framework and secondary mortgage market and high interest rates are still the major constraints towards the growth of housing and housing finance sector which is one of the potential key drivers of the economy.

5.0. Infrastructure Finance

The stock of infrastructure finance rose from Rs. 264 billion in Oct-Dec-10 to Rs. 296.5 billion in Jan-Mar-11 and with a slight dip settled at Rs. 290 billion – a 2.2% decrease from the previous quarter. The trend of financing in different sectors is topped by power generation sector as shown in detail in following sections.

The disbursement figure for this quarter was Rs. 6.7 billion and again the power generation sector remained the major beneficiary with 43.8% share. The NPLs have increased considerably over the year with Rs. 10.9 billion which were Rs. 7 billion a year ago.

The overall scenario did not present a rosy picture as shown by the financing trends. The importance of physical infrastructure cannot be overemphasized but the commensurate response is still lacking and leaving a lot to be desired. International experience emphasizes the need of institutional capacity for project development to achieve meaningful progress in infrastructure financing. All the developing countries have multiple institutions with varying degrees of mandate and functions peculiar to their economic needs but the common thread among them is they supply a pipeline of viable projects and means to provide long term fixed-rate financing.

5.1. Outstanding Portfolio

Total financing outstanding at close of Jun-11 was Rs. 290 billion against Rs. 296.5 billion at the end of previous quarter ending Mar-11. The volume of outstanding portfolio was Rs. 260 billion at the end of Jun-10.

The analysis shows, as in Figure 5a, that power generation sector stood out among all the sectors of infrastructure. A number of factors like power policy, availability of sovereign guarantees in case of IPPs, expertise of financial sector in this area and demand of energy are the main reasons of its consistent lead over the other sectors.

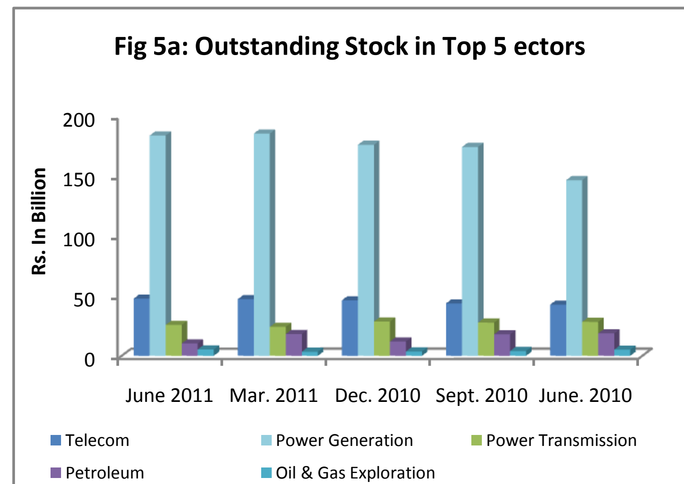


Figure 5a shows the quarterly position of top five sectors from Jun-10 to Jun-11. All the top five sectors showed a stabilizing trend in their respective volume of outstanding. However, the steep decline was witnessed in petroleum sector. The outstanding volume in this sector was Rs. 18.2 billion at the end of Mar-11 which reduced to Rs. 10.3 billion at the end of Jun-11.

5.2. Disbursements

Total of Rs. 6.7 billion were disbursed during April - June 2011 quarter in all infrastructure sectors against Rs. 7.6 billion in the previous quarter. The disbursement during April-June 2010 quarter was Rs. 10.3 billion. Figures 5b and 5c show the amount disbursed and share of each sector during the quarter under review.

Power generation sector received Rs. 2.9 billion, which is 4.8% of overall disbursement. Power generation sector got Rs. 6.4 billion in last quarter while it received Rs. 6.3 billion in April-June 2010

Fig 5c: Disbursement in Apr-June 2011

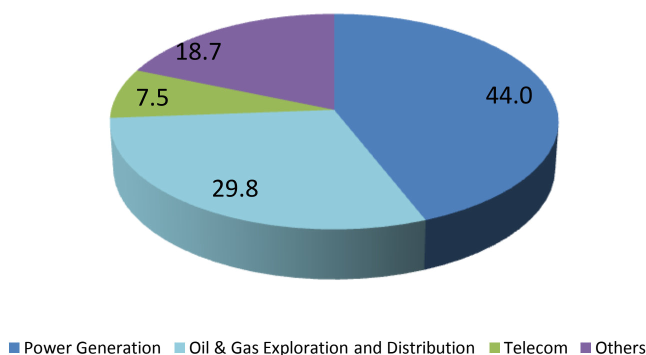
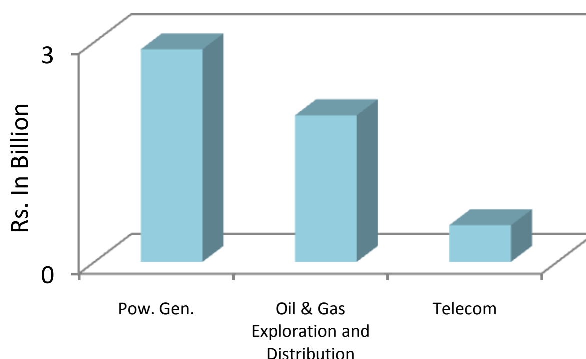


Fig 5b: Disbursements in Apr-June 2011



Oil & gas sector got revived after a quiescent phase of many quarters and received financing of Rs. 2 billion. This amount will be utilized to improve and enhance the distribution network of public sector gas utilities. Telecom sector also posted a minuscule Rs. 500 million financing. Telecom sector seems reaching a saturation point as most of telecom companies are in paying back mode and no new initiatives are on the ground.

5.3. Analysis of Sectoral Share in Infrastructure Finance Portfolio

Figure 5d & 5d' shows the comparison of top five sectors in outstanding infrastructure financing at the end of Jun-11 with the status existing on Jun-10. At the end of Jun-10, power generation sector had 56.3% of the total stock followed by telecommunication sector with 16.4%. After a year, the top slot continues to be held by power generation sector with a substantial 63.2% share in the pie. All other major sectors in graph showed a declining trend. The Telecommunication sector remained stable with 16.4% share. Petroleum sector, despite having huge

Fig 5d: Share in Outstanding Jun-11

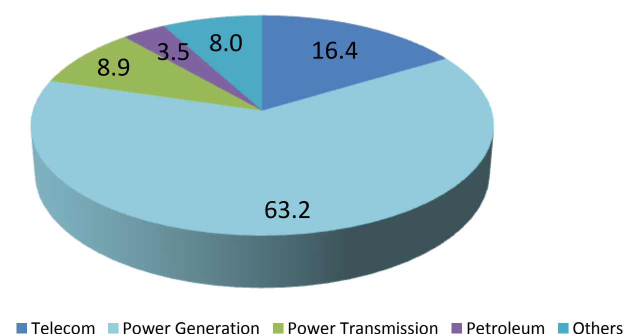
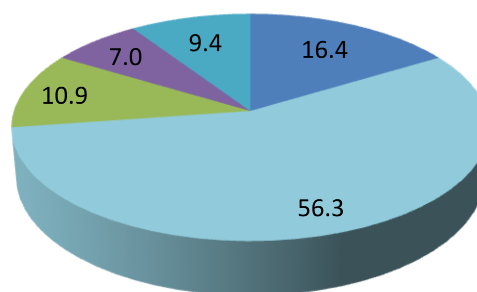


Fig 5d':Share in Outstanding Jun-10

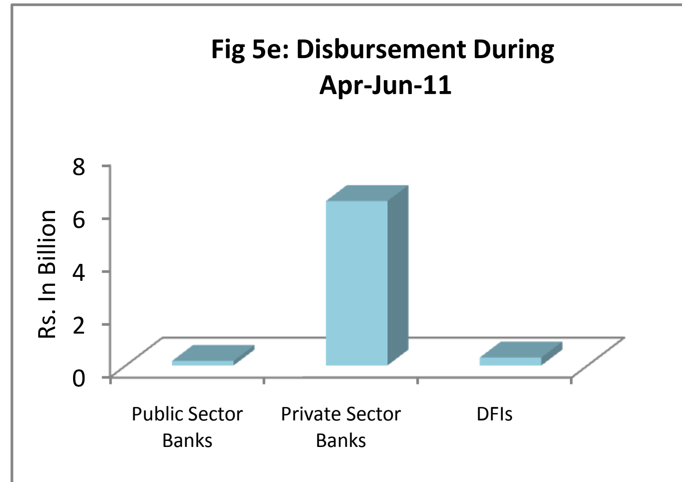


potential, had been on the downside from 7% to 3.5% in a year. The reduction of Power Transmission sector is

due to shifting of some of its outstanding to a power holding company.

5.4. Banking Sector-wise Disbursements

Figure 5e shows that private sector commercial banks disbursed Rs. 6.2 billion (90.0%) out of total Rs. 6.7 billion financing in infrastructure sectors during the quarter. Public sector banks disbursed Rs. 168 million (2.5%) while DFIs disbursed Rs. 309 million (4.6%) despite having a mandate of development finance. In same quarter last year, private sector banks disbursed Rs. 9.05 billion (87.9%) while public sector banks disbursed Rs. 1.07 billion (10.4%). DFIs' share in disbursements during the quarter ending Jun-10 was also minimal at Rs. 148 million (1.4%).

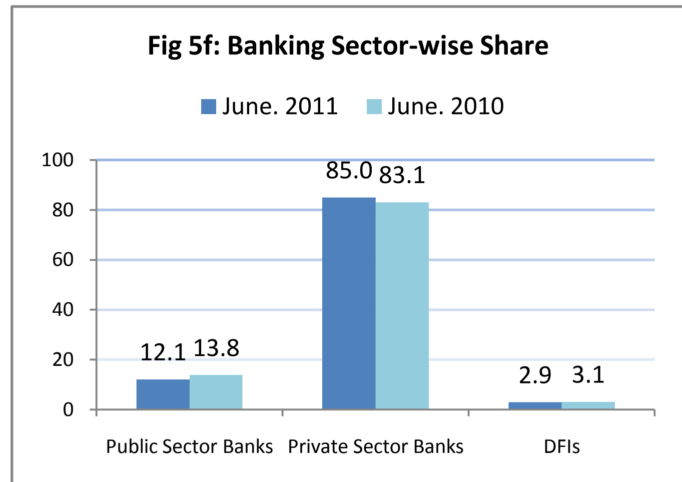


5.5. Banking Sector-wise Share in Outstanding

Figure 5f shows the category-wise share of banking sector in outstanding stock of infrastructure financing. The trend has been in favor of private sector as it was in previous quarters.

Share of private sector banks rose from 83.1% to 85%, while share of public sector banks declined from 13.8% to 12.1% after a year.

The share of DFIs remained below par through-out the year. Though private banks enjoy a major share, portfolio diversification beyond limited infrastructure sectors is highly desirable.



5.6. New Initiatives

The first ever wind power project of 49.5 megawatts (MW) in Pakistan having achieved all major milestones concluded the groundbreaking financial close in this quarter under review. The EPC contractor for the project has already initiated construction work on site. This is a landmark in wind sector of Pakistan achieved by the FFC Energy Limited under the facilitation of the AEDB, based on signing of Energy Purchase Agreement in April 2011 between M/s FFCEL and Central Power Purchasing Agency (CPPA) and Implementation Agreement with AEDB in February 2011. Pakistan now offers an investment-friendly and lucrative wind energy market for the investors and equipment suppliers. Now more than six (06) EPC contractors are ready to provide their services in Pakistan. The financing of projects have also become available with IFC, ADB, OPIC (Overseas Private Investment Corporation) and other commercial banks and financing institutions ready to finance wind power projects.

6.0. Key Development Finance Initiatives – Policy and Industry

Appreciating the critical role and significance of Development Finance for the sustainable economic growth in the country, SBP took the following key measures during the Quarter, Mar-11 to Jun-11

Revision in Credit Guarantee Scheme for Small and Rural Enterprises

SBP had earlier launched a Credit Guarantee Scheme (CGS) for Small and Rural Enterprises in March 2010. The scheme was modified in February 2011 and important features were made part of it; which include sharing 40 percent of bona-fide losses of PFI's credit portfolio, removal of interest rate cap and bifurcation into two components, introducing eligibility of farmers with economic landholding and increasing their loan size from Rs. 0.5 million to Rs. 2 million, giving definition of Small Enterprises and increasing loan limit from Rs. 5 million to Rs. 15 million. In this regard, limits have been allocated to eleven banks (PFIs) in the month of Apr-11. After necessary revisions in the CGS scheme, the PFIs are using the facility in an aggressive manner.

SME Training Programs

During the quarter under review, the following training programs were organized in coordination with DFSD SBP-BSC

- April 7-8, 2011 at State Bank of Pakistan SBP (BSC), Faisalabad
- May 2-3rd , 2011 at SBP (BSC), Gujranwala
- June 1-2nd , 2011 at SBP (BSC), Lahore
- June 22-23rd , 2011 at LRC, State Bank of Pakistan , Karachi

SME Market Segmentation in Pakistan

In order to develop profiles of key SME clusters, SBP, in collaboration with IFC, conducted **"SME Market Segmentation Study"** on 10 important SME Clusters of the economy. During the process, top 16 commercial banks were also involved and their feedback was incorporated in the study.

The project has been accomplished, and booklets published (http://www.sbp.org.pk/departments/ihfd-ifc.htm). Each booklet includes an industry overview and chapters on Market Assessment, Risk Assessment, Financial Benchmarking, proposed Banking Products for the sector **covering both Assets and Liability side**, and guidance on how these products could be channeled and distributed.

SCI – Pak and SBP Collaboration

In order to identify strategies to foster the communication and interaction among the SBP, financial institutions and SMEs in facilitating them access to finance to undertake energy and resource efficient (E&RE) production, a roundtable meeting was jointly organized by SBP and European Commission funded SCI-Pak Project in Karachi, in June, 2011.

Workshops for Promotion of Refinance Scheme in Flood Affected Areas

In order to revive SME's & Agricultural activities in flood affected areas, SBP in line with the Government relief measures, issued a Refinance Scheme vide SMEFD Circular No. 16 of 2010 for improving access to finance in 78 flood affected districts notified by National Disaster Management Authority (NDMA). The objective of the

scheme was to provide concessional financing to flood affected farmers through banks for agri. production/working capital finance in flood affected districts. The Scheme was announced on November 02, 2010 and will remain valid up to 31st October, 2011.

The scheme, however, could not achieve the desired results due to a number of issues, among which lack of awareness was the main factor. With a view to increase awareness among borrowers and increase utilization of SBP Schemes, SBP arranged Awareness Programs for the Flood affected areas, where, the target audience would be Regional Heads of banks, representatives of trade bodies and local chambers.

In this connection, five such awareness programs were held successfully at Hyderabad, Sukkur, Multan, Rawalpindi, and Peshawar on 6, 7, 9, 10 and 11th June, 2011 respectively.

Payment of 2nd Installment of Export Finance Mark-Up Rate Facility

SBP released 2nd installment of mark-up subsidy for the period ending 31-08-2010 under Export Finance Mark-Up Rate Facility & Mark up Rate Support for Textile Sector against Long Term Loans, vide IH&SMEFD Circular Letter No. 09 dated May 20, 2011.

Refinance Scheme for Revival of SMEs & Agricultural Activities in Flood Affected Areas

SBP expanded the scope and extended the validity of above Scheme, with a view to improve access to finance for SMEs and Farmers in the flood affected areas, vide IH&SMEFD Circular No.4 dated May 25, 2011. Now the scheme will also provide financing to the non-farm sector. Earlier, the financing under the scheme was allowed to farm sector only. Likewise, SBP has also allowed banks/DFIs to repay the principal amount of refinance within 15 days of the due date(s), instead of 7 days as allowed earlier under the scheme. The validity of the scheme has been extended up to November 30, 2012. Earlier, the validity of the scheme was 31st October, 2011.

LTFF Scheme – Eligibility of Packaging / Preservations of Food Items

In order to encourage export of Foods Items SBP had clarified that plant and machinery used in the export oriented projects for producing packaging material exclusively used in packaging / preservation of food items are also eligible under the Scheme, vide IH & SMEFD Circular Letter No. 12 dated June 27, 2011

Reduction in Export Performance Requirements under EFS-II

In order to facilitate the exporters of Hand Knotted Carpets, export performance requirement under EFS Part II for FY 2010-11 has been reduced to 1.50 times from 2.0 times.

Policy Adequacy and Awareness Seminars on Agri. Financing

In order to acquaint agri. graduates about the basic structure of agri. financing, related policies, schemes, initiatives taken by SBP in recent years to enhance the outreach of agri/ rural finance, SBP, in collaboration with SBP-BSC, banks, microfinance banks and agri. universities/ colleges, arranged “Policy Adequacy and Awareness Seminars on Agri. Financing” at University of Agriculture, Faisalabad on 16th May, 2011 and at Agriculture University Tandojam, Sindh on 19th May, 2011.

The participants were briefed about various tools & techniques of agri. financing including guidelines & schemes, products, processes, value chain of activities, forward & backward linkages, , etc. The speakers also responded to the questions from the audience and gave outline of the internship program at banks, specially designed for

agri. graduates. The seminars were attended by a large number of students, teaching faculty, academia, Chief Managers of SBP-BSC Offices, officials of DFSD, SBP-BSC and senior officials of banks.

Key developments as regards micro financing during the quarter

- The State Bank introduced certain amendments in the existing Branchless Banking Regulations vide BPRD Circular # 09 of 2011 dated 20th June 2011 with the objective of expanding the outreach of branchless banking operations. According to these amendments, SBP has introduced level '0' branchless banking (BB) accounts to bring the low income earning segment of society into financial services loop. The account opening process has also been simplified by allowing the agent to send the digital account opening form, customer's digital photo and an image of customer's CNIC to the FI electronically instead of hard copies. Similarly, the transaction limits of level 1 branchless banking account have been reasonably increased to cater to the needs of the customers by rationalizing the Know Your Customer (KYC) requirements. Now, all services permissible under existing branchless banking regulations shall be available to level "1" account holders.
- On May 08-09 2011, SBP hosted the two-day G2P Conference in collaboration with the UK Aid and World Bank arm, Consultative Group to Assist the Poor (CGAP) to discuss opportunities, synergies and challenges in automating G2P payments,. The conference drew an array of public and private sector speakers and audience including international donors, government agencies, banks, telecoms and solution providers.

- In the G2P Conference, the Governor SBP launched GBP 10 million Financial Innovation Challenge Fund (FICF) and unveiled the first round of FICF on Government to Person Payments (G2P). 'Banks, public sector institutions, Microfinance institutions, government agencies, pension funds, and academic institutions are invited to apply to promote G2P payment through bank accounts at branchless banking outlets and also provide other financial services to the G2P payments beneficiaries

- Financial Inclusion Program (FIP)

  To promote financial inclusion in the country, SBP has in place a comprehensive Financial Inclusion Program (FIP). The progresses on account of different components of FIP are given below:

  a. Microfinance Credit Guarantee Facility (MCGF) is in place with GBP 10 million, to incentivize commercial banks to provide wholesale funds to microfinance banks and institutions for on-lending to poor and marginalized groups. The MCGF has been able to mobilize wholesale funds of around Rs. 2 billion for the microfinance sector that will improve its outreach considerably. At end of 2nd Quarter FY11, MCGF deals worth Rs. 1,675 million have been made to 3 microfinance players.
  b. Institutional Strengthening Fund (ISF) worth GBP 10 million, is aimed to strengthen institutional & human resource capacity MFB/Is. So far grants of up to Rs.493.64 million have been approved for 13 microfinance providers (including one micro insurance agency) under 15 projects for addressing their institutional strengthening needs.

c. Pakistan Microfinance Fund (PMFF)
PMFF is a multi-donor credit enhancement fund. SBP in consultation with donors is probing into various alternative arrangements under which wholesale funding for on-lending purpose can be made available to microfinance providers on market based competitive rates to enhance market orientation and lessen dependence on grants and subsidies. At present, PMFF is in its feasibility phase, co-financed by SBP.

Implementation of Housing Advisory Group's Recommendations

As part of its earlier efforts, SBP had established a Housing Advisory Group (HAG) with an intention to conduct a thorough analysis of the existing regulatory and policy framework affecting housing finance. The HAG made number of recommendations stressing on the need to enhance access of financial services for the development of housing sector. These include reforms in legal and regulatory framework, establishment of secondary mortgage market, development of market intelligence, provision of affordable/low income housing finance products. SBP disseminated the recommendations to the concerned stakeholders and is currently coordinating with Provincial Governments, Pakistan Banks' Association (PBA), Association of Mortgage Bankers (AMB) and Association of Builders and Developers (ABAD) for implementation of some of the key recommendations.

Mortgage Refinance Company

Work on the establishment of Mortgage Refinance Company is being pursued aggressively. IFC developed a detailed business plan and feasibility for the Mortgage Refinance Company. Principal buy-in of the Ministry of Finance has been elicited and equity commitments from the GoP, commercial banks and HBFC have been received. Memorandum & Articles of Association of the proposed company have been developed and consultant is being hired to assist in incorporation of the company during the current financial year (2010-11).

Capacity building Program

In addition to initiatives taken to institutionalize housing finance, SBP realizes that a simultaneous development of human capital will play a critical role in ensuring sustainability of housing finance. Few training programs have been conducted on different aspects of housing finance including product development, loan marketing/distribution and origination & loan underwriting, servicing and risk management. Till date, approximately 400 bankers from over 20 banks have been trained in the mortgage business.

Development of Housing Finance Guidelines

To increase the efficiency of mortgage bankers, Housing/Mortgage Finance Guidelines have been developed, by adopting best international practices, and after consultation with internal and external stakeholders, including PBA.

A Presentation of IPDF's Approved Infrastructure Projects to Banks and DFIs

Infrastructure & Housing Finance Division, in its bid to bridge the gap between development and financing institutions of infrastructure projects, arranged a presentation of approved infrastructure projects developed by

IPDF (Infrastructure Project Development Facility) – a federal institution mandated with developing infrastructure projects under Public-Private Partnership mode.

The CEO of IPDF, Mr. Adil Anwar presented a number of approved projects to a select audience of banks and DFIs who have to play a significant role in providing financing to these projects. The presenter stressed the need for establishing a viability gap fund to make long-term project self-sustaining and also urged that our banking sector had great potential. The Director, IH & SMEF, Mohammed Mansoor Ali remarked that pension funds were also a potential source of funding long-term infrastructure projects. Additional Director, Mr. Imran thanked the audience and re-avowed the pledge of SBP creating a platform to ensure a synergetic approach towards infrastructure building.

7.0. Development Finance news from around the World

The following are some of the important news concerning Development Finance across the globe during the quarter, Mar-11 to Jun-11.

SBP, banks & SCI-Pak to develop network

http://nation.com.pk/pakistan-news-newspaper-daily-english-online/Business/16-Jun-2011/SBP-banks--SCIPak-to-develop-network

The State Bank of Pakistan, commercial banks and SCI-Pak may jointly develop an Energy & Resource Efficient (E&RE) network/ platform to address the financial needs of Small & Medium Enterprises (SMEs). This consensus was arrived at a Roundtable meeting which was jointly organized by SBP and European Commission Funded SCI-Pak Project in Karachi.

The roundtable also decided that awareness campaigns for SMEs should be launched at the grass root level to educate the masses regarding different financial instruments developed by SBP for the modernization of SMEs.

Driving innovation and growth: Small firms report university partnership success

http://www1.aston.ac.uk/about/news/releases/2011/june/university-partnership-success/

New research uncovers depth of relationship between higher education and SMEs in the Midlands, UK. Almost three-quarters (73%) of small and medium-sized businesses (SMEs) in the Midlands have worked with a university or higher education institution (HEI) in the past year, according to research published today by the Institute of Directors and Universities UK. The research, part of **Universities Week 2011**, reveals wide ranging engagement driving innovation and employment as well as boosting local economies.

IFC Helps Mongolian Bank Increase Capital and Lending to Small and Medium Businesses

http://media-newswire.com/release_1152426.html

IFC will provide $20 million to Khan Bank LLC, Mongolia's biggest bank by assets, to help strengthen its capital position and increase lending to small and medium enterprises.

IFC's seven-year subordinated loan will allow the bank to offer up to 14,000 new loans to small and medium enterprises by the end of 2015. IFC's investment will also help the bank maintain adequate capital and support its sustainability and development. IFC is the third-largest shareholder in Khan Bank, owning a 9.1 percent stake. Since becoming an IFC client in 2004, Khan Bank has grown to become the largest bank in Mongolia by assets and branch network, reaching about 80 percent of Mongolian households. More than 50 percent of its borrowers are women.

Businessmen ignorant of basic accounting concepts

http://www.indianexpress.com/news/businessmen-worth-crores-ignorant-of-basic-accounting-concepts/803728/

It came as a big surprise to the directors of micro, small and medium enterprises (MSME), department of industries (DI) when they realized businessmen — some of them successful for more than 20 years — were not even aware of the basic concepts of accounts. According to the directors, none of them knew how to read a balance sheet or the importance of preparing a project report of a company and much more. The directors are in the city to conduct a week long workshop on financial management for the industrialists.

The workshop began at the MSME office where 31 members of the Offset Printers' Association (OPA) participated. S S Bedi, Assistant Director, MSME and coordinator of the workshop said, "We understand the problem of the businessmen and that's why we arranged this workshop. Even last year one such workshop was arranged." The industrialists were urged to produce monthly balance sheets rather than annual ones and given tips on how to read them.

Trade office readies for SME development week

http://www.sunstar.com.ph/zamboanga/local-news/2011/06/14/trade-office-readies-sme-development-week-161096

A regional official of the Department of Trade and Industry (DTI) said preparations for this year's celebration of the national small and medium enterprise (SME) development week have been intensified as the date of the celebration draws near. Dr. Sitti Amina Jain, DTI assistant regional director, said the weeklong celebration will fall on the second week of July this year. This year's celebration is themed: "Pinoy SME: Business Tayo!"

Jain said that by bringing together potential and existing home-grown entrepreneurs and various SME stakeholders from all regions across the country, the event hopes to strengthen SME growth by gaining widespread support to the SME Development Plan for 2011-2016.

Insurance sector focus turns to small firms

http://gulfnews.com/business/banking/insurance-sector-focus-turns-to-small-firms-1.821598

Dubai: The insurance sector in the Gulf is all set to take up the cause of small- and mid-sized businesses in a big way. Global and regional insurers are equally interested in signing up to do so. AXA Gulf has confirmed plans to get into the SME space in a big way, with businesses in Saudi Arabia and the UAE being the primary focus, at least in the initial phase of the rollout.

The target is to have a 10 per cent coverage with SMEs on our annual gross premium written in three years." And AXA is getting the personnel to help them achieve the results. "One of the main challenges is to acquire the local flavor to reach out to SME clients," said Jerome Droesch, CEO for the Gulf and Middle East.

SME Star Program 2011 – search for outstanding entrepreneurs

http://www.sunstar.com.ph/zamboanga/local-news/2011/06/15/search-outstanding-entrepreneurs-starts-161304

The government, through the Department of Trade and Industry (DTI), has officially started its search for the country's outstanding entrepreneurs to give due recognition to the valuable contribution of small and medium enterprises (SME) to national economic development. Under the SME Star Program, three award levels or categories are included in the search.

These levels correspond to the stages in enterprise growth, such as SME Rising Star, SME Elite Star, and SME Presidential Star, said Manzur. The SME Rising Star category is for enterprises in the start-up and capability-building stage. It is conducted and awarded at the provincial level. The SME Elite Star is for enterprises at the domestic market penetration and export awareness stage and is awarded at the regional level. While the SME Presidential Star is for highly successful enterprises that have reached the export and expansion stage, which is awarded at the national level, Manzur said.

8.0. Special Section – Nexus between financial inclusion and financial integrity

FATF guidance on AML/CFT measures and financial inclusion

Financial inclusion is a multi-dimensional challenge, of which AML/CFT requirements are important aspect. Introduction of inappropriate AML/CFT requirements can negatively affect access to, and use of, financial services that may further generate new financially excluded groups. It is acknowledged that prevalence of a large informal, unregulated and undocumented economy negatively affects AML/CFT efforts and the integrity of the financial system. A pervasive cash economy can generate significant money laundering and terrorist financing risks. Dependence on informal financial services also limits access to reasonably priced credit and slows country's development. Moreover, if the funds are kept outside the formal system, there is a limited multiplier effect in the economy. One cannot ignore the fact that financial exclusion itself is a ML/TF risk. Solving the AML/CFT issue would be a milestone towards building an enabling framework for financial inclusion.

The Financial Action Task Force (FATF) has prepared a Guidance paper to provide support in designing AML/CFT measures that meet the national goal of financial inclusion, without compromising the measures that exist for the purpose of combating crime. The main aim of the document is to develop a common understanding of the complementarity of AML/CFT and financial inclusion and the flexibility offered by the FATF Standards through ***Risk-based Approach (RBA)***, to craft effective and appropriate controls. The Guidance paper reviews different steps of the AML/CFT process (Customer Due Diligence, record-keeping requirements, reporting of suspicious transactions, use of agents, internal controls), and for each of them presents how the Standards can be read and interpreted to support financial inclusion.

The general principle of a RBA is that where there are higher risks financial institutions (FIs) should take enhanced measures to manage and mitigate those risks, and that correspondingly where the risks are lower (and there is no suspicion of money laundering or terrorist financing) simplified measures may be permitted. The application of a risk-based approach requires countries to take appropriate steps to identify and assess the ML/TF risks for different market segments, intermediaries, and products on an ongoing basis.

It is important to note that financially excluded and underserved groups, including low income, rural sector and undocumented groups, in both developing and developed countries should not be automatically classified as presenting lower risk for ML/TF.

Presently, more than half of the world's adult population lack access to credit, insurance, savings accounts, and other formal financial services. There are many reasons why individuals may not take full advantage of mainstream financial service providers. However, the key is in finding alternatives delivery channels that work for specific context and which may differ depending on the target audience. It also relates changing financial habits. In that respect, one successful approach is to focus on changing how government payments such as wages, pension and social and medical benefits are delivered in both developed and developing countries.

Customer due diligence, verification and monitoring (Recommendation 5)

Regarding customer identification, FIs may apply differentiated CDD measures according to the profile of the (future) customer. Simplified CDD measures can be applied in cases where there is a demonstrated low ML/FT risk, but this should in no case amount to an exemption from or absence of CDD.

It is essential to distinguish between identifying the customer and verifying identification. Customer identification consists of obtaining information on the identity of the prospective customer. At this stage, no identification documentation is required to collect. In contrast, the verification of the customer identification requires collecting some documentation or checking a reliable, independent source documents, data or information that authenticates the veracity of the information obtained from the customer. The FATF does not provide further guidance on what the degree of reliability and independence of such documentation should be, although its exposure to fraud and counterfeiting is an important criterion for FIs to consider.

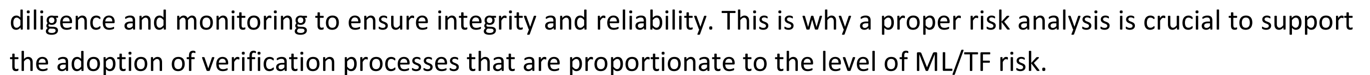
Passport or ID card is one of the methods used to verify the identity of customers in a majority of countries, it should be noted that the FATF Standards does allow countries to use other reliable, independent source documents, data or information.

The FATF Standards do not specify the exact range of customer information that the FIs subject to AML/CFT obligations should collect to properly carry out the identification process.

To further ease these requirements of CDD, some countries has extended the list of acceptable IDs such as expired foreign IDs, consular documents or other records that undocumented people can typically acquire in the host country (bills, tax certificate, healthcare document, birth certificates etc.). In India, if a person is not able to produce the normal identification documentation, banks may open an account, subject to: (i) introduction from another account holder who has been subjected to full CDD procedure with satisfactory past six month transactional history and is willing to certify photograph and address of the prospective customer or (ii) any other evidence as to the identity and address of the customer to the satisfaction of the bank. In the Philippines, for potential customers in rural areas, a Barangay Certification, issued by the elected head of a village, is accepted as a proof of identification and residence. In Malaysia, for rural areas which do not have any information of residency or address, the bank requires a postal address, which is either a communal post box or neighbor address.

Efforts to expand the range of reliable documentary types of identification have been supplemented in some developing countries by innovative IT solutions. Some countries are developing acceptable non-governmental and even non-documentary methods of verifying identification, such as a signed declaration from the community leader together with a photograph taken on a camera phone, biometrics or voice prints (such market-based solutions have been especially developed in the Fiji, Philippines and Malawi). Countries are also developing electronic multi-purpose forms of identification.

It is important to ensure that alternative identification processes do not create new barriers that further undermine financial inclusion. Every method of verifying customer identification requires some basic due



diligence and monitoring to ensure integrity and reliability. This is why a proper risk analysis is crucial to support the adoption of verification processes that are proportionate to the level of ML/TF risk.

In South Africa, authorities have considered developing products designed to serve the financially excluded or underserved people with residential addresses that could not be confirmed by reference to formal documentation. To introduce more simplified CDD, authorities introduced "Exemption 17", to release financial institutions from verification requirements in respect of products meeting specific requirements / conditions. The institutions still have to obtain and verify identity information, namely a customer's full name, date of birth and identity number. Exemption 17 facilitated the launch of several basic banking services including the Mzansi account and WIZZIT payments. Currently at least one in six banked people is active Mzansi customer. In India people without any acceptable form of identification are allowed to open "small account"

In relation to wire transfers, a so-called "progressive" or "tiered" CDD approach can be applied. This may imply for undocumented people access to financial services with very limited functionalities, with access to broader services being allowed only if the customer is able to provide further identification data.

It is important to highlight that there is no requirement, or expectation, that a risk-based approach must involve a complex set of procedures to put it into effect; the particular circumstances of the business will determine the most appropriate approach. Whatever approach is considered most appropriate to the firm's money laundering/terrorist financing risk, the broad objective is that the firm should know who their customers are, what they do, and whether or not they are likely to be engaged in criminal activity or to be conduit for proceeds of crime. However, there is no one-size-fit-all approach. A risk assessment will often result in a stylised categorisation of risk: e.g., high/medium/low. The FATF has identified examples of customers, transactions or products that may present a lower risk of ML/TF and to which simplified CDD measures may be applied.

The process of reliance on third parties with respect to CDD is permitted under the FATF Standards (Recommendation 9). In certain countries (such as Australia), consulates, embassies, police officers, licensed doctors, certain teachers, etc. can be third parties that financial institutions may rely upon to carry out some CDD functions. In such scenarios, financial institutions are required to satisfy themselves that a third party is adequately subject to AML/CFT regulation and supervision by a competent authority and has measures in place to comply with the CDD requirements.

Monitoring refers to manual or electronic scanning of transactions. The degree and nature of monitoring by a financial institution will depend on the size of the financial institution. The principal aim of monitoring in a risk-based system is to respond to enterprise-wide issues. Monitoring under a risk-based approach allows a financial institution to create monetary or other thresholds below which an activity will not be reviewed. Even in the case of lower risk customers, monitoring is needed to verify that transactions match the initial low risk profile and if not, trigger a process for appropriately revising the customer's risk rating. In some countries, the choice has been made to mitigate the risk introduced by simplified CDD by closely monitoring transactions linked to the relevant products and accounts. However, if little CDD is undertaken, scanning may not be able to deliver significant benefit in the absence of a sufficient range of available information.

Record-keeping requirements (Recommendation 10)

The record keeping requirement under the FATF standards does not require the retention of a photocopy of the identification document(s) presented for verification purposes but merely that the information on that document be stored and kept for 5 years. A number of countries, such as the United States, Australia and Canada, have considered but rejected imposing photocopying obligations on their regulated institutions. They decided against that for a number of reasons, for instance that the photocopies could be used to commit identity fraud; that they may breach privacy laws and that they may reveal information about the client that could form the basis of discriminatory practices, for instance the refusal of credit facilities to that client.

Recommendation 10 allows different forms of documents' retention, including electronic storage which is particularly useful in the context of mobile phone banking. Depending on the size and sophistication of mobile provider's record storage, the following record retention techniques are acceptable: 1) Scanning the verification material and maintaining the information it electronically; 2) Keeping electronic copies of the results of any electronic verification checks; 3) The option of merely recording reference details

In South-Africa, for instance, legislation allows for electronic capturing and storage record information, including in relation to documents of which copies have to be retained. In Rwanda and Kenya, storing electronic finger prints is permitted and in both of these countries credit unions have piloted fingerprint identification technology for rural poor customers.

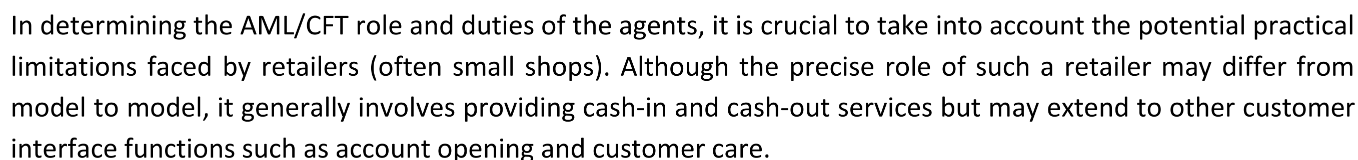
Report of suspicious transactions (Recommendation 13)

The risk-based approach will enable financial institutions to direct additional resources at higher risk areas, but once a suspicion has been formed, RBA is not applicable. A risk-based approach is, however, appropriate for the purpose of identifying suspicious activity.

Use of agents (including recommendation 15, 23 and special recommendation VI)

The use of agents to distribute financial services is part of an increasingly popular model for financial inclusion in many countries. In these countries, banking and payment services are provided through mobile phones and small retail outlets, such as groceries, bakeries, etc.

Normally customer identification and verification obligations are carried out by officers or employees of the financial institution. However, depending on the jurisdiction, and having regard to the diversity of the financial sectors, there may be occasions when these functions are permitted or are in practice performed by agents. An agent can be equated with the financial institution's employee in the sense that the agent is like an extension of the financial institution, and the conduct of CDD by these agents is treated as if conducted by the principal financial institution. The principle of ultimate liability of the financial institution for agents' compliance with the AML/CFT requirements seems almost universal although the extent of liability may differ from one country to another.



In determining the AML/CFT role and duties of the agents, it is crucial to take into account the potential practical limitations faced by retailers (often small shops). Although the precise role of such a retailer may differ from model to model, it generally involves providing cash-in and cash-out services but may extend to other customer interface functions such as account opening and customer care.

Few countries permit agents to conduct CDD, and agents routinely verify customer identity. In many countries, agents' ability to conduct CDD measures is limited to certain lower risk financial products.

It is important to note that, in the context of SRVI, it is not the practice in most countries to impose independent AML/CFT obligations on the agents of the remittance services instead, the principal, as a regulated institution, remains solely responsible for meeting the AML/CFT obligations, including for the actions (and omissions) carried out by its agents. This seems consistent with the general FATF approach of treating agents as an extension of the financial institution, and not as something entirely separate from it.

Supervision and oversight will primarily focus on the principal financial institution, but could include onsite oversight visits to agents. The degree of monitoring of the agents will be based on the perceived risks, both external and internal, associated with the agent, such as the products or services being provided, the location and the nature of the activity. The risk-based approach requires a higher level of monitoring to locate and stamp-out few agents that knowingly or through willful blindness act in a way that may conceal their customers conduct from routine monitoring. The degree and nature of agent monitoring will depend on the transaction volume and principal volume of the agent with whom the principal financial institution shares responsibility for effective AML/CFT, the monitoring method being utilized (manual, automated or some combination), and the type of activity under scrutiny.

Internal Controls

Financial institutions must develop an effective internal control structure, including suspicious activity monitoring and reporting and create a culture of compliance, ensuring that staff adheres to the financial institution's policies, procedures and processes designed to limit and control risks with some degree of flexibility having regard to the ML/TF risk.

9.0. Development Finance - Outlook

The total outstanding portfolio of Development Finance (DF) sectors declined to Rs. 826.9 Billion, registering decline of 1.6 percent at the end of Jun-11. However, non performing loans (NPLs) of DF sector saw a marginal decrease from Rs. 163.9 billion to Rs. 162.5 billion at the end of the period under review, recording a quarterly decline of 0.8 percent. The decline in DF portfolio may be attributed to prevailing economic slowdown, power outages, domestic law & order situation, natural calamities, and overall shyness of the industry towards the sectors.

However, despite the prevailing adverse conditions, there still exists a strong reason for a positive course of action to take place, as a result of greater realization on the part of SBP, GoP, the banking industry and other stakeholders, to play a more effective role for the development of the subject sectors. Further, the huge potential of the DF sectors itself is a highly motivating factor to encourage the stakeholders to tap on, and consequently develop it for the benefit of economy and their own business interests.

Thus, going forward, a positive turnaround is probable provided the relevant stakeholders play their role in a more meaningful and effective manner. However, it would be unrealistic to expect a change that could bring drastic improvement in the overall economic situation in general and DF sectors in particular; as rising inflation, poor law and order situation, natural calamities and dependence of the government on budgetary borrowings from the banking sector harms positive growth in the DF sectors of SMEs, Micro, Agriculture, Infrastructure and Housing.

The State Bank, on its part, has taken various important initiatives for the development of the DF Sector that will cause positive impact on the availability of funds for the sector and its overall development in the long run. Some important initiatives include improvements in Credit Guarantee Scheme for Small & Rural Enterprises, Refinance schemes for flood affected districts, Microfinance Credit Guarantee Scheme, Refinance Scheme for Revitalization of SMEs, Scheme for modernization of SMEs, Cluster Profiling Surveys, introduction of Branchless Banking, Mortgage Refinance Company and Capacity Building/Awareness Programs for the stakeholders.

Development Finance reviews published by SBP

Development Finance Quarterly Review (Jun-2011)
Development Finance Quarterly Review (Mar-2011)

Development Finance Review (Dec-2010)
Development Finance Quarterly Review (Sep-2010)
Development Finance Quarterly Review (Jun-2010)
Development Finance Quarterly Review (Mar-2010)

Development Finance Review (Dec-2009)
Development Finance Quarterly Review (Sep-2009)
Development Finance Quarterly Review (Jun-2009)
Development Finance Quarterly Review (Mar-2009)

Development Finance Review (Dec-2008)
Development Finance Quarterly Review (Sep-2008)

These Reviews are available at
http://www.sbp.org.pk/SME/DFG.htm