Guidelines

for

Livestock Financing

STATE BANK OF PAKISTAN
Agricultural Credit Department
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1. Introduction

Agriculture is the most important sector of our economy that contributes 23 percent to the GDP, employs 42 percent of labour force, accounts for more than 60 percent of exports and provides raw material to most of the industrial and manufacturing base of the country. Livestock is the largest sub-sector of the agriculture accounting for 47 percent of value added of the sector and constitutes about 11 percent to the GDP. While the disbursements to the agriculture sector has witnessed an appreciable rise during the last few years as a result of sector friendly policies of State Bank of Pakistan (SBP), the livestock sub-sector could not get its due share in the substantially enhanced flow of credit to the sector. During the fiscal year 2005, the Agriculture sector fetched credit of Rs108.7 billion, out of which the share of livestock was only Rs 6.8 billion or 6.2 percent of the total disbursements.

In view of the significance of the sector in terms of contribution to GDP & employment and importance to serve as a vehicle to alleviate poverty rampant amongst the rural population where livestock is bred and maintained, the SBP established a Committee of Experts in August, 2005 to come up with some strategy for increasing share of institutional finance to this neglected sub-sector of agriculture albeit having huge potential for growth. In light of the recommendations of the Expert Committee and input from the stakeholders including banking sector and MINFAL, SBP has framed 'Guidelines for Livestock Financing' to facilitate and encourage Banks/FIs in enhancing credit flow to the livestock sector. The Guidelines cover all areas of the livestock financing business including products development and their review, purposes and objectives of the loan, eligibility of borrowers, delivery channels, monitoring mechanism, etc. Banks may adopt the guidelines in its present form or with some adjustments that suit their organizational needs and market characteristics.

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

2. Guidelines for Dairy and Meat Farm Financing

Dairy and meat farms constitute a significant portion of the livestock sector. Pakistan is the fourth largest producer of milk in the world, however, only 2-3 percent of milk is processed. Similarly, the country has great potential to develop meat farm and can have substantial share in the attractive Halal meat market. Lack of access to adequate financial services has been among other key impediments in the growth and development of this sector. The banks can benefit from the guidelines to tap the sector that promises high returns to the dairy growers, banks and the economy as a whole. The easy and sustained access of dairy and meat farms with affordable financial services would enable the dairy and meat growers to acquire modern and efficient livestock facilities, infrastructure and processing systems for milk and meat production thereby giving boost to livestock sector to produce large quantity of livestock products for domestic consumption as well as for export.

3. Types of Financing

The dairy and meat farms need financing facilities for their daily expenses i.e. working capital requirements and long term investment for purchase of buffaloes, cows, goats, sheep, dairy and meat farms equipments, construction of sheds, etc. The guidelines discuss three broad types of financing for the dairy and meat farms viz. Working Capital, Term Finance and Composite Loans.

3.1 Working Capital Financing

To meet the day to day expenses of the borrowers in livestock, banks can extend the working capital financing to cover following items:

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

3.2 Term Financing

The term finance facilities could be provided for the purposes of:

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

3.3 Composite Loans Facility

Composite Loan Facility is designed specifically for small dairy and meat growers. Salient features of the facility are as under.

- These loans are aimed at attracting small dairy and meat growers who constitute a bulk of livestock growers in the country and are generally hesitant to avail credit from banks.
- The composite loans would contain term finance as well as working capital to cater to the needs of small livestock holders for purchase of milch animals, young calf, goat, sheep for fattening etc. and 1-3 months feed or overhead expenses.
- The banks should design simple products for this market with the minimum possible documentation and repayments compatible with their cash flows from all sources.
- Such loans may be repayable in a period of upto 5 years in monthly instalment including a grace period of upto three months.

4. Eligibility of Borrower

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

- The borrower should be a holder of computerized NIC.
- The borrower should not be a defaulter of any bank/ Financial Institution. This condition may be relaxed in case the ACO/ branch manager is satisfied with the creditworthiness of the borrower and that the earlier default was circumstantial and not wilful.
- ACO/branch manager/ regional manager are satisfied and comfortable with the farmer's and guarantor's (where applicable) identity, character, reputation & creditworthiness.
- The borrower must be living in the area for 5 years or more. However, this condition may be relaxed with the level of satisfaction of the ACO/ branch manager to the background, character, capacity and repute of the borrower.

It is advisable that the ACO has detailed understanding and information about the borrower, his capacity to effectively use and repay the loan and land, building and other capital assets he/she owns, etc.

5. Fixation of Loan Limits and Repayment Terms

The limit amount may be assessed by the ACO/branch manager on the basis of financing request appraisal or feasibility report. The banks should take due diligence and market survey to assess the prices of feed, cows, buffaloes, goats, etc. Following parameters are recommended for this purpose:

5.1 Financing for Working Capital

Purpose	Indicative, Financing/ Loan	Mark- up Repayment	Maximum Period
Dairy Farm			
i. Dairy and meat farms overhead including purchase and plantation of animal fodder and feeds, labour, electricity, vaccination, medication & health care, artificial insemination, etc. and low cost durables like utensils for animal feeding, calf feeders, feed grinders, tokas, feed mixing machines and feed or milk containers, bangles, rope/iron chains, etc	Maximum 180 days working capital needs	Monthly, based on the limit or amount utilized during the month	Limit to be extended for one year to be renewed or rolled over each year based on the following: • Loan account is regular • No mark-up payment is overdue • At least 6 out of the 12 months mark-up payments received within 10 days of the due date • Payments equivalent to at least 15% of the maximum amount utilized, have been received during the year
	Meat Farm		
	Maximum 180 days working capital needs	Quarterly, based on the limit or amount utilized during the quarter	Limit to be extended for one year to be renewed or rolled over each year based on the following: • Loan account is regular • No mark-up payment is overdue • At least 2 out of the 4 quarters mark-up payments received within 10 days of the due date • Payments equivalent to at least 15% of the maximum amount utilized, have been received during the year
ii. To finance receivable against deferred bills	80% to 90% of the deferred bills (in order to cover both principal and accrued mark-up)	Through realization of the deferred bills	Each deferred bills amount to be cleared within 90 days of financing or discounting

5.2 Term Financing

Purpose	Indicative Financing/ Loan	Repayment	Maximum Period
Dairy Farm			
i. Purchase of mature milk yielding buffaloes/ cows or replacement thereof	Maximum 80% of actual cost	Monthly	Upto 5 years including grace period upto 3 months
ii. Purchase of young animals for rearing for dairy purposes	Maximum 80% of actual cost	Monthly	Upto 5 years including grace period upto 3 months
iii. Milk storage chilling tanks or plants and milk carrying containers (To be allowed for Dairy farms having more than 20 animals)	Maximum 80% of the purchase price/ cost (average of at least 3 quotations)	Monthly	Upto 5 years including grace period upto 3 months
iv. Distribution vehicles (motorcycles, pickups, refrigerated vans) (To be allowed for Dairy farms having more than 20 animals)	Maximum 80% of the purchase price/ cost (average of at least 3 quotations)	Monthly	Upto 5 years including grace period upto 3 months.
v. Construction or procurement of permanent sheds, water tanks. Purchase of utensils for animal, water pump, generator and tube well	Cost should be assessed by banks evaluator. Maximum 80% of the purchase price/ cost (average of at least 3 quotations)	Monthly	Upto 5 years including grace period upto 3 months
Meat Farm			
i. Purchase of young buffaloes, cows, sheep and goats for rearing for meat purposes or replacement thereof	Maximum 80% of actual cost	Quarterly or half yearly	Upto 5 years including grace period upto 3 months
ii. Refrigerated meat storage and refrigerated containers	Maximum 80% of the purchase price/ cost (average of at least 3 quotations)	Quarterly or half yearly	Upto 5 years including grace period upto 3 months
iii. Distribution vehicles (pickups & refrigerated vans)	Maximum 80% of the purchase price/ cost (average of at least 3 quotations)	Quarterly or half yearly	Upto 5 years including grace period up to 3 months
iv. Construction or procurement of permanent sheds, water tanks, purchase of utensils for animal, water pump, generator and tube wells	Cost estimation should be assessed by banks evaluator. Maximum 80% of the purchase price/ cost (average of at least 3 quotations)	Quarterly or half yearly	Upto 5 years including grace period upto 3 months.
v. For processing of livestock by-products, such as animal casing/gelatin units, bone processing units, rendering plants, etc.	Cost estimation should be assessed by banks evaluator. Maximum 80% of the purchase price/ cost (average of at least 3 quotations)	Quarterly or half yearly	Upto 5 years including grace period upto 3 months.

5.3 Composite Loans for Small Dairy & Meat Farms

Purpose	Indicative Financing/ Loan	Repayment	Maximum Period
Purchase of cattle and other items eligible for term finance and working capital needs for 1-3 months	Maximum 80% of actual cost	Monthly , with 3 months grace period	Upto 5 years including grace period upto 3 months

6. Mark-up

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

7. Security and Collateral

i) **For loans upto Rs.5 Lacs**

Primary security

- Personal Surety

Secondary security (at the discretion of the bank)

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

ii) **For loans exceeding Rs.5 Lacs.**

- Hypothecation of animals, as in case of loans upto Rs.5 Lacs.
- Secondary collateral (at the discretion of the bank) and indicative margin requirement there against are as follows:

Collateral and Margin Requirement

Collateral	Margin Requirement
Mortgage of agriculture land* & rural, urban or commercial property.	30 % of market value
Pledge of SSC/DSC, etc. Lien on bank deposits.	0% of encashment value, covering principal and 6 months mark-up.
Pledge of gold and gold ornaments.	25% of valuation by the bank's approved gold smith. (Mark to market annually)
Individual / Group / NGOs guarantee.	1. Should provide coverage to Principal alongwith one year mark-up. 2. Maximum per person exposure as mentioned in Prudential Regulations for Agriculture Financing regarding personal guarantee.

*Market value of land would be assessed by the ACO/branch manager by visiting the site and collecting necessary information about the land.

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

8. Channels of Financing

- Direct financing to dairy or meat farms.
- Indirect financing to dairy or meat farms through milk or meat processing units, etc.
- Financing against deferred bills issued by reputed milk or meat processing units.
- Discounting of deferred bills.

Further details about the loan delivery mechanism and marketing of loans may be seen at Appendix.

9. Documentation

Following documents or formalities must be completed:

- Bank account in the name of intending borrower before applying for the finance facility.
- Standard Application Form (SBP format) in Urdu along with borrower and his/her father / husband name in English (for feeding in computer with correct spelling) duly completed, should be obtained. Signatures/thumb impression of the applicant, guarantor and witnesses (where required) and verified by the branch manager.
- In case of tenants / harees a certified copy of Khasra Girdawari, Fard Jamabandi or Form VII & VII A (for landowners of Sind Province).

or

- Bank charge may be created on the agriculture land through passbook system by the Revenue Authorities and a charge creation certificate Schedule - II is to be obtained.

or

- Registered or Equitable Mortgage of rural/urban property **or** earmarking of Bank's Deposits, **or** pledge of DSC/SSC/Regular Income Certificates/other financial instruments **or** pledge of gold, silver and gold and silver ornaments.
- Letter of agreement-cum-guarantee (IB-7) from the borrower.
- Appraisal report on the applicant and credit report of the guarantors must be prepared before finance is sanctioned.
- SBP Credit Information Report should be obtained.
- For loans against the continuing guarantee and charge on fixed / current assets of the processing units. The processing units will provide a list of their bonafide milk providers along with their computerized NIC numbers and addresses. Finance would be disbursed in the account of milk processing unit for onward

disbursement to their milk providers. The processing unit will be responsible for repayment of loan as per terms and conditions agreed between the bank and the processing unit.

- Completion of documentation shall be the responsibility of ACOs or branch/regional managers.

10. Conditions and Covenants

- Submission of Financial/Income & Expenses Statements should be encouraged.
- Submission of periodic inventory record at least on quarterly basis.
- For Financing more than 50 cows / buffaloes or 100 sheep/goats the following should also be observed:-
  - Submission of product marketing plan for next six month on bi-annual basis.
  - Feed procurement source, quantity & pricing plan on biannual basis.
  - Vaccination through doctor authorized by branch/regional manager.

11. Loan Monitoring System

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

12. Recovery of Loans

First recourse for the bank to recover its loans is the borrower and his/her cash flows. The effective monitoring system, follow-up and frequent interaction with the borrowers is critical for ensuring recovery of agricultural loans. The traditional correspondence and letter/notice based recovery mechanism will not be successful in agricultural loans. Considering the low tickets and large volume nature of agricultural and rural credit it would not be effective to send payment request letters particularly to the small clients. However, in case of delinquent borrowers the following recovery process may be initiated:

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

13. Special Precautions

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

14. Non Performing Loans (NPLs)

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

Appendix

Guidelines for Marketing of Agriculture (Livestock) Loans and Monitoring Mechanism

i) Delivery Channels

a) Direct financing to livestock owners/farmers

- The traditional commercial banking approach of waiting for the clients to visit branches to avail financial services normally doesn't work for agricultural (livestock) loans. The banks therefore will have to devise innovative and cost effective mechanism to reach to the clients and market their products.
- The branch / area managers should develop a comprehensive database about the area/region the branch is supposed to serve consisting of the numbers of districts towns, union councils, villages in the area and their demographic data; the total cultivatable area, major crops, fruits, vegetables, the livestock statistics, number of dairy farms, meat farms, cattle breeding farms; average number of cattle in each household; the level of presence of other Financial Institutions (FIs), etc.
- The ACOs/MCOs should be assigned the union councils and villages to be covered during a specified period along with the portfolio build-up targets.
- The ACOs/regional managers should arrange meetings with the villagers/farmers, livestock growers to introduce the products and services they are offering for the farm, non-farm and livestock sectors.
- The meetings should be arranged in consultation and collaboration with the active and influential persons of the village/area like Mosque Imams and Chaudrays etc. so that maximum number of villagers could be informed about the products. The meeting should be focused, standardized and time bound.
- After the introductory meeting the ACO should follow-up with the interested farmers/dairy growers for extending farm and non-farm products.
- The branches in rural areas or in small towns adjacent to rural areas should be designated as Agricultural and Rural Finance Branches and given specific business targets for agricultural credit and encouraged to become more and more mobile to market the bank's agricultural products.

b) Indirect lending/ financing

- Indirect lending may be made through milk processing units, sweetshops, biscuit manufacturers, milk collection firms, retail milk shops, chocolate manufacturers, yogurt and cheese manufacturers, ice cream manufacturers, ice cream parlors, etc.
- The banks may either provide loans to the milk processors for onward lending to livestock growers on guarantee of the processing units etc or directly to the growers against the deferred bills issued by the processing unit.
- The wholesale funds to the processing units will however, be properly secured against charge on the assets of the processing unit, mortgage of rural/urban properties etc.

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

ii) Monitoring Mechanism

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

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

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