CREDIT GUARANTEE SCHEME FOR SMALL AND RURAL ENTERPRISES

Background

Small and Medium Enterprises (SMEs) play an important role in the economic development of a country as majority of the enterprises operating in a country are either small or medium entities. According to an estimate, around 90% of the total enterprises operating in Pakistan fall in the category of SMEs. Thus, the growth of small and medium businesses is imperative for a developing country like Pakistan. There is a need to improve access to formal finance for this sector, particularly, small and rural enterprises.

Realizing the importance of this sector for economic growth and to improve access to formal sources of finance, State Bank of Pakistan has launched, in collaboration with Federal Government and UK's Department for International Development (DFID), Credit Guarantee Scheme (CGS) for Small, Rural and Micro Enterprises. Key features of Credit Guarantee Scheme for Small, Rural & Micro Enterprises are given below.

Selection of Participating Financial Institutions (PFIs)

State Bank will select commercial banks, microfinance banks (MFBs) and leasing companies to serve as Participating Financial Institutions (PFIs) and allocate Credit Guarantee Limits (CGLs) to each PFI. The banks, MFBs and leasing companies to be considered as PFIs shall be in a reasonably good financial condition and shall have considerable share/expertise in small enterprises/agricultural/micro-enterprise financing.

Eligibility of Borrowers

The borrowers under the Scheme will be micro and small enterprises and farmers with economic landholding without any specific regional or cluster restrictions, across the country. The borrower shall preferably be a fresh customer; however, an existing borrower can also be extended additional lending facility under the Scheme. PFIs are encouraged to serve collateral-deficient borrowers under CGS and may amend their credit policies for this purpose. The selection criteria for eligible borrowers will include:

- ✓ Regular and estimable positive cash flows to ensure ability of debt servicing
- ✓ Conformance to Prudential Regulations for SMEs/Agri/Micro Financing
- ✓ Clean e-CIB record

Risk Sharing with the Financial Institutions

60 percent risk coverage shall be provided for loans extended to:

a) Start up businesses,
b) Women borrowers, and
c) Small and Rural enterprises operating in under-served areas of the country with respect to SME financing.

For eligible borrowers, other than those mentioned above, the risk coverage to PFIs under the Scheme shall be linked with the value of the underlying collateral and shall operate in the following manner:

Risk Coverage	Collateral Value
60 Percent	Clean Lending
40 Percent	Value of Collateral upto 100 percent of loan
20 Percent	Value of Collateral Greater than the Loan Amount

In cases, where a loan falls in two categories, higher risk coverage shall prevail.

Guarantee Structure

The PFIs will be allocated a guarantee limit on annual basis that would define the total guaranteed amount of a PFI under the Scheme. PFIs shall report to DFSD, SBP BSC, Head Office all individual cases against which guarantee is solicited. Individual loans extended by PFIs after the allocation of CGL, which meet the eligibility criteria, shall be guaranteed to the extent of the allocated guarantee limit. PFIs shall manage the total loan exposure against the guarantee limit ensuring that guarantee requests submitted to SBP remain within the allocated limit. The issuance of Credit Guarantee is subject to compliance with provisions of the Guarantee Scheme and other instructions issued by the State Bank from time to time, as deemed necessary. PFIs shall ensure that the guaranteed loans are not used for purposes contradicting the very objective of the Scheme, i.e. the facility will not be used for debt swaps/adjusting an existing loan, buying company shares or financing interest payments etc. SBP/SBP BSC have the right to withdraw any approval of guarantee if it is discovered at any stage that the borrower was not eligible for financing under the Scheme at the time of extension of the loan facility. In such an event, respective PFI will bear 100 percent credit risk of such borrower.

Pricing of Loans under the Guarantee Scheme

PFIs shall apply market-based mark-up rate under the Scheme. However, in cases where SBP has provided a refinancing facility (such as SME Refinancing Facility for BMR), mark-up rate allowed by SBP to PFIs under the particular facility shall prevail.

Loan Limit and Tenure of the Guaranteed Amount

Small enterprises (SEs) may be extended financing for a maximum tenor of 5 years and upto the maximum amount allowed under SBP’s Prudential Regulations for Small Enterprises.

Microfinance Banks may extend loans from Rs. 150,000 to Rs. 500,000 to Micro Enterprises for a tenor not exceeding 5 years.

Farmers may be extended financing under the Scheme upto the maximum amount of Rs two (2) Million. The maximum loan tenor allowed for the purchase of tractors and other agri loan implements under the Scheme is 5 years. However, in order to avoid portfolio concentration in tractor and other implements financing, the aggregate financing under this category shall not exceed 20% of the total allocated guarantee limit of the bank. For purchase of agri inputs, maximum loan tenor under the Scheme is 3 years.

Sector Specific Approach under CGS

In order to create Developmental Impact on Small and Rural Enterprises, PFIs shall adopt a sector specific approach. For this purpose, out of the total allocated limits, PFIs would lend 30% to specific sectors identified by them, starting from July, 2015, which will increase to 50% in 2017 (Jan-Dec). The limits of only those PFIs will be enhanced in future which will fully utilize their sector specific limits. Moreover, PFIs would be required to intimate to SBP, 3-5 sectors for the purpose.

Applying for Guarantee Cover

The borrowers to be covered under the Guarantee Scheme shall be issued a unique Customer Identification Number (CIN) by PFIs in the form of 'PFI-xxxxxx-yyy' where 'PFI' is the abbreviated/acronym reference of the PFI, 'xxxxxx' is the six digit number issued to each successive customer in ascending order and 'yyy' is the three digit loan number for the customer. For example XYZ Bank Limited may issue 'XYZ-000025-001' as CIN against the first loan given to its 25th customer under the Scheme.

Each PFI shall nominate at least two senior officials in their head office as Authorized Contact Officials/ Signatories (ACOs) to communicate with the Development Finance Support Department (DFSD), SBP BSC and Infrastructure, Housing & SME Finance Department (IH&SMEFD) State Bank of Pakistan, Karachi. PFIs shall convey the duly verified signatures along-with names, designations and contact details (phone, mobile, fax, email) of nominated ACOs to both DFSD & IH&SMEFD. Only those guarantee/ claim requests of PFIs shall be entertained under the Scheme which are signed by nominated ACOs.

PFIs shall apply on quarterly basis, within 15 working days of respective quarter end, for the guarantee facilities for the borrowers who were extended lending facilities during the previous quarter. The applications for guarantee facility shall accompany a covering letter requesting for the facility and duly filled-in format CG-1 (attached as Appendix I). Both the covering letter and duly filled-in format shall be signed by nominated ACOs. Each PFI shall have the primary responsibility of ensuring that its total guaranteed loans do not exceed its allocated CGL at any point in time. After ensuring that all the conditions specified in the Scheme have been complied with, DFSD will intimate the concerned PFI regarding issuance of guarantee through Issuance of Guarantee Letter.

Each PFI shall report its outstanding position of all previously guaranteed loans on quarterly basis, within 15 working days of respective quarter end, as per the format CG-2 (attached as Appendix II).

Payment of Claims under the Guarantee Scheme

Claims shall be paid to PFIs on case to case basis upto the guarantee coverage provided against a particular loan once the loan is categorized as 'Loss'. Objective classification criteria as defined in the relevant Prudential Regulations of SBP shall be followed to categorize a loan as 'Loss'. PFIs shall lodge claims on quarterly basis, within 15 working days of respective quarter-end, against all loans falling under the 'Loss' category in the previous quarter as per the format CG-3 (attached as Appendix III) duly audited and authenticated by their Internal Audit Department. PFIs would also attach the e-CIB reports of the individuals cases for which claims would be lodged.

DFSD shall internally scrutinize the claims in the light of information submitted by PFIs to assess any deviation and seek clarification from concerned PFI, if so required. In case the claim is as per the instructions of the Guarantee Scheme, DFSD shall reimburse the guaranteed amount within 15 working days after receipt of complete information relating to the claim request.

Recoveries

Re-imbursement of guarantee claim shall not obviate PFIs from the right of recovery of the defaulted amount. PFIs shall continue with their regular procedure for recovery of loans. The proportionate share of SBP in any recovered amount under the Scheme may be deposited with SBP BSC on quarterly basis. Recovered amount should be deposited by last date of the respective quarter. The status of recovered amount shall be reported to DFSD, SBP BSC on quarterly basis, within 10 working days of respective quarter end, through CG-4 (attached as Appendix IV). Any recovery from a delinquent borrower after reimbursement of guarantee claim by SBP is to be treated as recovery of principal, while the costs incurred on recovery efforts is not to be passed on to the Guarantee Scheme.

Reporting Timelines

PFIs shall be required to submit on quarterly basis, or as and when required, reports of their financing to micro, small & rural enterprises for evaluation of compliance of all the processed cases with the criteria of the Scheme. The following table provides a summary of all quarterly reporting requirements under the Scheme:

S. No.	Report Name	Caption	Timeline
1.	Form CG-1	Report of Fresh Guaranteed Loans by PFI	Within 15 working days after respective quarter end
2.	Form CG-2	Report of Existing Guaranteed Loans by PFI	Within 15 working days after respective quarter end
3.	Form CG-3	Claims on Guarantee Fund	Within 15 working days after respective quarter end along with e-CIB report
4.	Form CG-4	Report of Recoveries from Delinquent Guaranteed Borrowers	Reimbursement: By last date of the respective quarter Reporting: Within 10 working days after respective quarter end

Monitoring of the Guaranteed Portfolio

On the basis of the quarterly data reported by PFIs, DFSD, SBP BSC will monitor the performance of PFIs viz-a-viz their allocated limits on quarterly basis and more frequently if deemed necessary. Further, to ensure compliance with the objectives of the Guarantee Scheme and avoid adverse selection problems on part of PFIs, Banking Inspection Departments of State Bank will review the guaranteed loan portfolios of PFIs during their regular inspection of PFIs. Moreover, BID-I and BID-II will pay special attention to the claims lodged by PFIs under the Scheme during their regular inspection of the bank in order to ensure that the lodged claims were genuine. In case any deviation in the reimbursed claims of PFI is found during inspection, the amounts of such claims shall be debited from the account of the concerned PFI maintained with the SBP BSC.

Interpretation

If any question/query arises in regard to the interpretation of any of the provisions of the Scheme or of any directions or instructions or clarifications given in connection therewith, the decision of SBP shall be final.

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