

*Annexure-A of IH&SMEFD Circular No. 04 dated March 21, 2022*



**State Bank of Pakistan**

# **Challenge Fund for SMEs**

**Expression of Interest  
Document**

**March 21, 2022**

# Challenge Fund for SMEs

## 1. Background

Small and Medium Enterprise (SME) sector plays a significant role in the economic development of country. This sector is considered as the backbone of any economy. As per the estimates of Small & Medium Enterprise Development Authority (SMEDA), there are more than 5 million SMEs in Pakistan. SMEs contribute 40% in GDP of Pakistan and 25% in overall exports. After Agriculture sector, SME sector provides employment to highest percentage of working population in the country. SME sector contributes to 78 % of non-agriculture sector employment. SMEs are one of the main sources to reduce poverty, expand national economy and job creation. Due to various regulatory measures and facilitative role played by SBP, SME financing started rising from 2013. The outstanding SME financing reached Rs 524 billion in December 2021 as compared to Rs 284 billion in December 2013.

However, structural barriers still exist which impede bank lending to SMEs, like information asymmetries, high transaction costs and lack of tangible collateral for availing loans by the SME owners and entrepreneurs.

## 2. Financial Inclusion & Infrastructure Project (FIIP)

To support the implementation of Pakistan's National Financial Inclusion Strategy (NFIS), the World Bank Group (WBG) has approved a Financial Inclusion and Infrastructure Project (FIIP) for Government of Pakistan. Improving access to financial services for microenterprises and SMEs (MSMEs) is one of the key focus of this project. It especially seeks to substantially increase access and usage of digital financial services by SMEs.

## 3. Challenge Funds for SMEs (CFS) – General Guidelines

Providing innovative and digital financial solution for SMEs is one of the priority of SBP. Therefore, SBP is launching a Challenge Funds for SMEs (CFS) to find and support innovative solutions for SME banking in the country.

It is the need of the hour to effectively utilize the technological innovative solutions that give access of financial services to businesses especially to small business. The objective is to use innovation to make markets inclusive so that SMEs in Pakistan have access to electronic/online business solutions in hassle free manner.

The goal of CFS is to encourage banks to develop innovative technological solutions to cater the banking needs of SME sector. This will help increase the access and usage of financial services by SME sector. Going forward, it can play a major role to digitize financing and payments.

## Challenge Fund for SMEs

### a. Objective

SBP is launching a challenge fund to spur innovations in areas such as sustainable business models that ride on utilization of technology or other alternative delivery channels and products & services tailored for SMEs. This will focus on financial innovations leveraging the use of technology (including Fintech).

Digital SME banking includes a broad range of financial services accessed and delivered at affordable cost through digital channels. It can be a catalyst in improving living standards by providing affordable financing options and encourage entrepreneurship. It is estimated that the market potential of Digital Finance Services in Pakistan will cross US\$ 36 Billion by 2025, providing a 7% boost to the GDP, creating 4 million new jobs and resulting in US\$ 263 Billion new deposits<sup>1</sup>. This potential can only be achieved through a robust and efficient Digital Financial Services (DFS) ecosystem. In this regard, SBP is focusing on leveraging technology not only in payments but also modernizing lending platforms. SBP is also promoting an enabling regulatory environment for new players and forming new contractual relationships between financial institutions and third parties.

The CFS aims to support banks to leverage technology and innovation to develop new or amend existing financial products & services and delivery platforms that will enhance access to finance to SME sector. The purpose of this challenge fund is to help;

- develop and implement innovative ideas to increase financial inclusion of SMEs
- develop user friendly and cost effective innovative banking solutions for business entrepreneurs
- develop and integrate key offerings with other players in the banking system with interoperability option
- novel solutions to create easy digital access to formal financial services including savings products, lending services, pensions, insurance tools, remittances, etc.

### b. Potential areas for grant under CFS

The CFS provides an opportunity for banks to experiment with/implement innovative digital banking products & services to improve access to finance to SMEs either individually or in collaboration with Non-banking financial institutions (NBFIs)/ Fintech/ Electronic Money Institutions (EMIs)/ software houses. NBFIs, Fintechs, EMIs and software houses hereinafter are referred as collaborating institutions. The scope of CFS will focus, but not be limited to the following areas:

- SME banking solutions
- Digital payment solutions for SMEs

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<sup>1</sup> Mc Kinsey Global Report, "Digital Finance for All: Powering Inclusive Growth in Emerging Economies" September, 2016

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- Developing E-Commerce / market place
- Digitizing Loans application and credit management

The above mentioned area will focus to enhance financing to SMEs sector with more focus on marginalized segments such as starts-ups, women led SMEs and underserved areas.

### c. Operational Mechanism

#### i. Fund Management

Infrastructure, Housing & SME Finance Department (IH&SMEFD), SBP will serve as CFS-Secretariat. A cross-functional team having technical level representation from SBP's relevant departments (such as IH&SMEFD, AC&MFD, BP&RD, PSP&OD and DI&SD) to manage the initial scrutiny of the proposals. After having initial evaluation, the shortlisted proposal will be presented to Evaluation Committee to be chaired by Executive Director-Development Finance Group (ED-DFG). The Committee is composed of representation from IH&SMEFD, PSP&D and AC&MFD. SBP reserves the right to make final decision.

#### ii. Submission/ approval of proposals

Applicant banks may submit their complete proposals to CFS-Secretariat. Upon a thorough desk review/initial scrutiny of the proposals by cross functional team, CFS secretariat will present proposals to the Evaluation Committee. The Committee after analyzing the proposal including its deliverables and impact on SME financing will accord approval along with financial assistance to pilot test the innovation.

#### iii. Duration and Size & Cost Participation

Grant size will be determined according to the financing requirements of the proposal under consideration. However, each grantee will contribute 15% of the total cost. Depending upon the quality & innovations of proposal, the grant size can vary from project to project basis. However, one bank will get one grant only. The duration of the projects should be ideally not more than 8 months.

#### iv. Monitoring

The CFS-Secretariat will monitor the progress through monthly/quarterly progress reports submitted by grantees. The quarterly reviews will present three key aspects of projects, including progress on work plan, outcomes and grant utilization. The project's progress will be seen over two/four months and in case of signs of failure or dissatisfaction; the project funding may be ceased.

#### v. Knowledge exchange

The grantees are expected to share project experiences in the form of regular reporting, contribution to newsletters, presentations and conferences.

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### 4. Eligibility Criteria

Commercial Banks (conventional & Islamic) are eligible to apply for CFS. The banks can also apply in partnership with any collaborating institution. However, lead responsibility will rest with applicant bank. The banks will be required to fulfil the eligibility criteria as defined below:

Sr. No.	Qualification Criteria	Evaluation Parameter	Mean of Verification
1	Interested bank must be compliant to standard Minimum Capital Requirement prescribed by State Bank of Pakistan from time to time.	Mandatory Criteria	Annual and Quarterly Financial Statements.
2	Interested bank must not be rated as “marginal” or “un-satisfactory” under CAMELS and CAELS supervisory framework in the last available supervisory onsite/ offsite assessment.	Mandatory Criteria	Latest available CAMELS or CAELS supervisory ratings will be used for assessment.
3	Collaborating institution must be registered with tax authorities and appear on Active Taxpayer List of FBR (where applicable).	Mandatory Criteria	Copies of valid Tax registration certificates / NTN Certificates. FBR Website proof of Active Taxpayer List (where applicable).
4	The collaborating institution should not be blacklisted/ debarred/ sanctioned by any organization/ agency and information provided in proposal response / submission is correct.	Mandatory Criteria	Affidavit on PKR 100 stamp paper from the bank confirming that: <ol style="list-style-type: none"> <li>1. All the information provided by the bank is correct;</li> <li>2. Name of collaborating institution is not included in the World Bank/PPRAs /NACTA debarred/sanctioned list.</li> <li>3. Name of collaborating institution is not</li> </ol>

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			included in the UN sanctioned list.
5	The product, service or solution must be designed to be implemented in Pakistan.	Mandatory Criteria	
6	The product, service or solution must be backed by some demand side evidence, demonstrating its viability against an existing challenge faced by the target market.	Mandatory Criteria	

### 5. Proposal Evaluation Criteria

Broadly, the CFS Evaluation Committee will analyze the proposal based on feasibility, relevance and impact on SME financing. The applicant must clearly demonstrate how the product, service or solution has transformational potential impact on number of borrowers, SME financing portfolio (outstanding) and other banking solution.

Sr. #	Score Based Evaluation Criteria		Max. Score
	<b>SME Financing Portfolio</b>		<b>100</b>
1	Applicant Bank should have SME financing portfolio (max. score=40)	<b>Small Enterprise Financing</b> 1. Financing > Rs 20 billion =20 marks 2. Financing > Rs 10 &< 20 billion = 15 marks 3. Financing > Rs 5 billion &< 10 billion = 10 marks 4. Financing < Rs 5 billion = 5 marks	20
		<b>Medium Enterprise Financing</b> 1. Financing > Rs 30 billion =20 marks 2. Financing > Rs 15 &< 30 billion = 15 marks 3. Financing > Rs 5 billion & < 15 billion = 10 marks 4. Financing < Rs 5 billion = 5 marks	20

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2	No. of SME borrowers (max. score = 30)	<b>Small Enterprise Financing</b> 1. No. of borrowers > 10,000 =15 marks 2. No. of borrowers > 5,000 and < 10,000 =10 marks 3. No. of borrowers > 1,000 and < 5,000 =5 marks 4. No. of borrowers < 1,000 = 2 marks	15
		<b>Medium Enterprise Financing</b> 1. No. of borrowers > 2000 =15 marks 2. No. of borrowers > 1000 and < 2000 =10 marks 3. No. of borrowers > 500 and < 1000 = 5 marks 4. No. of borrowers < 500 = 2 marks	15
3	SME financing as percentage of bank's private sector financing	1. > 10% = 10 Marks 2. >7% < 10% = 8 Marks 3. >5% and <7% = 5 Marks 4. <5% =3 marks	10
4	Growth in SME Financing Portfolio in past 4 years (Since December 2018)	1. > 20% = 10 Marks 2. >10% < 20% = 08 Marks 3. <10% = 5 Marks 4. < and equal to 0% =3%	10
5	NPL portfolio as of December 31, 2021	1. < 10% = 10 Marks 2. >10% < 20% = 05 Marks 3. >20% = 02 Marks	10

### 6. Terms & Conditions

- Interested banks shall submit only one expression of interest (EOI), either individually or in partnership with collaborating institution.
- The interested banks shall bear all costs associated with the preparation and submission of their EOI.
- The EOI prepared by the banks, as well as all correspondence and documents relating to the EOI exchanged by the banks and the SBP shall be in English or Urdu.
- At any time prior to the deadline for submission of proposal, the SBP may, for any reason, whether at its own initiative or in response to a clarification requested by a prospective bank, amend the CFS proposal. Amendments will replace/supersede earlier CFS proposal.
- SBP reserves the right to make final decision.

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### 7. Format and Submission of Proposal

Proposal should be submitted as per format appended at annexure-B of IH&SMEFD Circular No 04 dated March 21, 2022 and should reach to CFS Secretariat latest by April 18, 2022.

### 8. Reporting & Coordination

The main point of contact from SBP during execution of CFS project will be:

Mr. Akhtiar Ahmed  
Senior Joint Director  
Infrastructure, Housing & SME Finance Department  
State Bank of Pakistan Karachi  
Ph: +92-21-99221951

### 9. Ownership of Confidential Information

The grantee(s) bank would ensure that all the data/ information collected under CFS grant is kept confidential and will be the sole and exclusive property of SBP. The grantee will not, acquire any right, title or interest in or to any of the confidential information collected for this project.

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