

## **Mark up Subsidy and Guarantee Facility for the Rice Husking Mills in Sindh**

### **Introduction:**

State Bank of Pakistan has issued SMEFD Circular No 7 of 2010, according to which, refinancing facility is provided to banks against lending to SMEs for modernization of their units. The modernization may take the form of establishing new units or undertaking BMR of the existing units. The rates charged to the borrowers are 8%, 9% and 10% for the tenures of 3, 5 and 10 years respectively.

The Sindh Enterprise Development Fund (SEDF), Government of Sindh, in collaboration with SBP, has offered further subsidy on the use of funds under the Scheme to the **rice-husking mills in Sindh**. The subsidy is in the form of reducing the end user rate further to 2.75%, and offering guarantee cover to banks to bear their credit loss against principal outstanding amount to the extent of 30%.

The SBP current rate for end user under the scheme is 9% with banks' margin being 2.75% for loans of 5 year's tenure. Under the proposed facility, the end-user rate will be 2.75%, i.e. the difference of 6.25% will be borne by SEDF.

The above subsidy (reduced mark-up and guarantee cover) will be governed under the existing SBP re-financing Scheme issued through SMEFD Circular No 7 of 2010; with the following additional features:

#### **1. Mark-up Subsidy:**

Under the Scheme, the facility will carry a mark-up burden of 9% as already stipulated under the Scheme for tenor of 5 years; however, the borrower (end-user) will be charged only 2.75%, i.e. the remaining 6.25% will be borne by the SEDF.

#### **2. Partial Guarantee:**

In addition to the Markup Subsidy, the SEDF will also provide partial credit guarantee cover of 30% to banks through SBP against their outstanding loans (principal portion only) under the Scheme.

#### **3. Eligibility under the Scheme**

- The loan facility under the Scheme will be available for establishment and BMR of **Rice Husking Mills in Sindh Province**.
- Financing shall be available for a maximum period of 5 years including a maximum grace period of six months.
- Maximum loan size for a single borrower shall not exceed Rs 10 million (Rupees Ten million only) under the Facility.

#### **4. Selection of PFIs:**

State Bank in consultation with SEDF will select 3-4 commercial banks from among the applicant banks to serve as Participating Financial Institutions (PFIs), and allocation of limit will accordingly be made to each PFI. The banks to be considered as PFIs would be in reasonably good financial condition and having considerable branch network in the concerned area.

#### **5. Procedure for allocation of Limits:**

- i. The banks which have already been allocated refinance limits under the Refinance Scheme for Modernization of SMEs, may apply for **guarantee-cum-subsidy** limit within their refinance limits, and submit their requests to State Bank of Pakistan within 7 working days after issuance of these instructions.

- ii. State Bank of Pakistan will evaluate banks' requests and allocate limits to them in light of their eligibility and availability of funds from SEDF.

**6. Establishment of Subsidy & Guarantee Fund:**

- i. State Bank of Pakistan will convey the approved limits to SEDF and upon receipt of commensurate funds from SEDF to meet guarantee and subsidy of limits, State Bank of Pakistan will convey allocated limits to the banks.
- ii. State Bank will also convey allocated limits to the Development Finance Support Department (DFSD), SBP BSC (Bank) which will serve as the guarantee and subsidy office
- iii. The guarantee and subsidy funds deposited by SEDF will be placed in a separate account maintained in SBP BSC (Bank), Karachi. The Funds of the Scheme will also be managed by DFSD

**7. Procedure for banks to avail the Facility:**

- i. In case a borrower for which the bank desires to avail refinance facility under the refinance scheme also qualifies the eligibility criteria of this scheme, may forward loan case of such a borrower to SEDF with the request to issue letter of comfort for sanctioning of the *facility*.
- ii. The concerned bank will submit its request for refinance to the concerned SBP BSC office as per the terms and conditions outlined in the refinance scheme. However, in order to obtain facilities for eligible borrowers under this Scheme, concerned bank will forward its request for guarantee and subsidy facilities along with Letter of Comfort provided by SEDF to the DFSD through the same field office of SBP, BSC (Karachi, Hyderabad, and Sukkur).
- iii. The SBP BSC offices will subsequently also intimate approval of refinance to the DFSD in respect of all loans for which banks have forwarded their requests for guarantee and subsidy facilities through that office.
- iv. The primary responsibility for eligibility of borrowers for the guarantee and subsidy facility rests on the bank which sanctions the loan facility to the borrower. The DFSD shall assess compliance with terms of the Scheme in light of the documents submitted by the concerned SBP BSC office/bank and confirm the Guarantee and Subsidy facility keeping in view the limit of the financing bank.
- v. The DFSD shall, however, have the right to withdraw its confirmation of guarantee and subsidy if it is identified through inspection/ verification that the borrower was not eligible for facilities under this scheme at the time of extension of the loan facility. In such an event, the PFI shall bear 100% of the credit risk and also return the subsidy amount disbursed for such borrower.
- vi. The DFSD shall convey issuance of guarantee and subsidy facility for a loan to the concerned bank through relevant field office of SBP BSC (Bank) within 7 working days after receipt of complete information from the SBP BSC (Bank) and/or the concerned bank.
- vii. Under the Scheme, SBP will recover its outstanding principal amount lent under the facility on due dates from the banks' accounts maintained with it as per the procedure outlined under the Refinance Scheme. However, the mark-up portion of 6.25% will be recovered by SBP from the funds placed with it by SEDF till the time guarantee is not invoked by the bank.

**8. Guarantee Facility:**

- i. The underwriting standards, internal controls and monitoring mechanism of banks should be strong enough to cater to the issues of adverse selection.
- ii. Banks shall lodge claim of guaranteed amount after a loan is classified as "Loss" under the PRs for SME Financing.

- iii. The lending branch of the bank shall submit their claims for reimbursement as per the prescribed Claim Format duly audited and authenticated by their Internal Audit Department to the DFSD through its relevant SBP BSC office.
- iv. The SBP BSC office will note the submission of claim for its own information purposes and forward the guarantee claim to the DFSD within 2 working days.
- v. After receipt of claim request, the DFSD shall internally scrutinize the request in the light of information submitted by bank and will reimburse guaranteed amount (i.e. 30% of the outstanding principal amount) by providing requisite funds to the relevant SBP BSC office with necessary instructions for transfer of funds to the concerned bank.
- vi. The re-imburement of claim by State Bank shall not obviate lending bank from right of recovery of the defaulted amount. The banks shall continue with their regular procedure for recovery of loan and status shall be reported to the SBP SBC on six monthly basis. Any amount recovered will be treated as recovery of principal and will be apportioned among the Guarantee Fund (SEDF/SBP) and the lending bank in the ratio of 30:70.
- vii. State Bank of Pakistan shall stop recovery of mark-up subsidy amount from the guarantee and subsidy account from the date of reimbursement of guarantee claim to the concerned bank.
- viii. The SBP BSC Field office will start recovery of mark-up subsidy portion of 6.25% from the concerned bank along-with principal outstanding amount as per the repayment schedule from the date of approval of guarantee claim.

**9. Interpretation:**

If any question arises with regard to interpretation of any instructions of the Facility, the decision of the SBP shall be final.

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