Appendix – I

LOAN POLICY

– FY 2019

Table of contents

LOAN POLICY – FY 2019

1 OVERVIEW

1.1 *PREFACE*

The significant role played by the Micro, Small and Medium Enterprises [MSMEs] in the Indian Economy is well known. MSMEs make significant contributions to India's Gross Domestic Product [GDP], manufacturing output, exports and employment generation. The MSME sector is the second largest contributor to country's GDP. MSMEs also help address geographic disparities through dispersal of entrepreneurial activities. They are considered to be the nurseries for entrepreneurship, often driven by individual creativity and innovation. MSMEs are important for the national objectives of growth with equity and inclusion.

In order to address the challenges of the MSMEs to scale up their performance and competitiveness, the Bank has adopted a multi-pronged approach to meet their requirement of capital, term credit, working capital, receivable finance, infrastructure (in clusters), etc., through various instruments/products of assistance.

1.2 *FRAMEWORK OF THE LOAN POLICY*

ThePolicylays down the broad approach, which the Bank adopts in respect of different credit processes, credit risk management, control and monitoring and is supplemented by specific circulars, manuals, guidelines issued from time to time. The policy will be amended from time to time in the light of changing business and economic environment and will be reviewed annually.The focus of the Loan Policy is on qualityasset growth coupled with growth in net income in each segment of business while maintaining the focus on customer needs.

TheBank would also pursue the ways for generating non-interest / fee based income. As regards indirect finance business, cautious dispensation of credit with regard to state level institutions would continue.

The Loan Policy covers all lending of the bank in rupee as well as foreign currency. Operations under Bank's Treasury, Fund of Funds and Promotional & Development activities are excluded from the purview of this policy[1].

[1]Exposure caps would be applicable to Credit operations and Treasury

The Bank would provide financial assistance to MSMEs for the eligible activities, irrespective of the nature of constitution of the enterprise. Accordingly, assistance could be extended by the Bank to an individual, proprietorship, association of persons, partnership firm, limited liability partnership, company, society or trust.

1.3 *OBJECTIVES OF THE LOAN POLICY*

The broad objectives of the Loan Policy of the Bank are outlined hereunder:

(i) To build and sustain a high quality portfolio well diversified in terms of clients, markets and products with an acceptable risk adjusted yield.

(ii) To establish a comprehensive credit strategy to fulfill the corporate mandate as per the SIDBI Act, 1989, amended from time to time, and undertake all such activities, directly or indirectly, that supports the MSME sector.

(iii) To pursue product innovation by the Bank based on market requirements.

(iv) To promote inclusive growth through micro finance.

(v) To strengthen the risk management systems for appropriate pricing of credit risks and ensure close monitoring of the credit portfolio.

(vi) To build strong alliances with intermediaries for tapping new business areas.

1.4 *OVERVIEW OF LOAN POLICY*

The strategy for lending takes into account the Bank's approach for developing a healthy credit portfolio, its management and risk mitigation. Accordingly, the Loan Policy of the Bank broadly covers the followingaspects:

- Credit Management Policy
- Business Policy of Verticals
- Credit Risk Management

1.5 *VALIDITY/ AUTHORITY OF LOAN POLICY*

The Loan Policyis the principal document for the credit operations of the Bank, duly approved by the Board of Directors and is expected to serve as the guiding document for lending operations of the Bank.

This Loan Policy shall remain in force till the next revision is carried out and disseminated, which will be on annual basis.

All Verticals / Operating Offices shall act upon this Policy. Clarifications / further guidelines, if needed, would be issued by Risk Management Vertical (RiMV)/concerned Business Vertical.

The Loan Policy guidelines will be applicable to all the facilities extended to various customers.

The Bank will abide by all the guidelines, directives and advices of Reserve Bank of India as may be in force from time to time. The product verticals would align their guidelines/ master circulars relating to the products, procedural aspects of credit appraisal, processing, sanction, documentation, etc. with the Loan Policy framework.

2 CREDIT MANAGEMENT POLICY

The business development strategy would be supported by a prudent Credit Management Policy. The market demand to improve products & processes would be balanced with exercise of sufficient control on the credit delivery processes so that exercise of prudence is not sacrificed.

2.1 *THRUST BUSINESS AREAS*

The Bank has identified the following to be the thrust business areas:

- Institutional lending viz. resource support / refinance to banks/ Financial Institutions [FIs], and non-banking financial companies [NBFCs], Small Finance Banks [SFBs],public financial institutions [PFIs]and public sector undertakings [PSUs]etc. benefiting MSME sector.
- Assistance to microfinance institutions [MFIs]
- Sectors under important missions of the Central Government such as “Make in India”, “Zero Defect Zero Effect” and “Digital India” etc.
- Green finance to promote environmental sustainability through energy efficiency, cleaner technologies and adoption of renewable energy etc.
- Co-lending with Banks and other financial intermediaries
- Cluster level interventions
- Services Sector

While the Bank will maintain its emphasis on financing thrust areas, it shall continue to provide assistance to all eligible MSMEs to meet their various fund and non-fund requirements.

2.2 *MICRO, SMALL and MEDIUM ENTERPRISES*

The definitions adopted for manufacturing and service sector activities are as indicated under Micro, Small and Medium Enterprises Development [MSMED] Act, 2006 as modified by Government of India [GoI] from time to time. The extant definitions under MSMED Act, 2006 are as under:

Enterprise Category	Manufacturing (Original Investment in P&M)	Services (Original Investment in Equipment)
Micro	Up to `25 lakh	Up to `10 lakh
Small	Upto `500 lakh	Upto `200 lakh
Medium	Upto `1000 lakh	Upto `500 lakh

For manufacturing enterprises, a list of equipments to be excluded for ascertaining the eligible investment in plant and machinery is notified under MSMED Act.

The activities being financed/to be financed by the Bank, would include enterprises eligible under the definition of MSMED Act, both manufacturing and service enterprises and also, other service sector projects as approved by the Bank with focused approach on the MSME linkages of the assisted projects.

The Bank also extends assistance to existing customers of SIDBI which would graduate out of the MSME category with the said assistance from the Bank, with appropriate checks to be defined by the Product Vertical.

2.3 *PRODUCT MANAGEMENT*

2.3.1 **Benchmarksfor Sanction:**

The benchmarksfor sanction[BfS] as applicable to various products of the Bankare given in **Annexure I**. Relaxation cap has also been prescribed against BfS norms. Proposals upto the relaxation cap can be approved by the delegated authority. However, in respect of renewals at current level or reduced level, delegated authority may relax the BfSnorms, beyond relaxation caps specified for the respective Committees,provided suitable risk mitigants are put in place.

Further, Central Credit and Investment Committee [CCIC] - CGM for proposals up to the delegation of Regional Credit, Settlement and Investment Committee [RCSIC], CCIC - DMDfor proposals up to the delegation of CCIC-CGM and in other cases, Executive Committee [EC], can consider relaxations beyond the cap prescribed in the Policy [except Prudential Rating and sector specific norms as indicated in para 6.2.2] on the merits of individual credit proposals. However, such relaxation may be accorded only under exceptional circumstances and rationale for seeking such relaxations/deviations together with risk mitigation measures are suitably brought out in the appraisal memorandum.

Further, additional risk premium, if any to be charged for such relaxations, would be decided by the delegated authority.

2.3.2 Facilitation for Product Development/Innovation

The Bank has put in place a suitable mechanism to understand the business needs of the MSME customer / beneficiaries[including IFV and SFMC products] and address them swiftly. Accordingly, Product Innovation and Review Committee [PIRC] at the HO level would considerand recommend/ approvenew products and modifications to existing products/ processes.

Apart from approving products, PIRC would also approve structuring of specific arrangements in a cluster or around a large corporate/ OEM where several MSMEs are expected to be benefited. Such arrangements could have different dispensations than those followed for regular credit products.

PIRC would function as per details given in Para No. 3.3.5 of the Enterprise and Risk Management (ERM) Policy.

2.3.3 Coverage under Guarantee schemes

The credit facilities to the eligible MSE customers may be generally covered under guarantee schemes operated by Credit Guarantee Fund Trust for Micro and Small Enterprises [CGTMSE], National Credit Guarantee Trustee Company [NCGTC] etc., as applicable.

2.3.4 Cross-selling with Government Schemes

The products of the Bank would also be dovetailed with the schemes of GoI and State Governments, wherever feasible, to improve the viability of the assisted projects and growth in overall asset base of the Bank.

2.4 *PROCESS MANAGEMENT*

2.4.1 Delegation of Powers

The key tool for managing the internal processes of the Bank is the Delegation of Powers [DoP] to variouscommittees and the individual functionaries of the Bank. It also puts in place suitable system of checks and balances in the creditand investment related decision processes.

2.4.2 Appraisal process

The credit proposals for term loan and working capital assistance to MSMEswould be appraised inCredit Appraisal and Rating Tool [CART]. However, credit proposals falling under Secured Business Loan [SBL], asset light[2] and other cash flow based financing categories, infrastructure and any other new products may be appraised outside CART in Detailed Appraisal Note [DAN].

In view of relatively high delinquency levels in certain sectors, the Bank would adopt a cautious/selective approach for financing under these sectors with better risk mitigation. Currently these sectors are textiles, drugs & pharmaceuticals, hotels, leather & leather products, food & food products, power including windmill & solar, hospitals and iron & steel. The list may be modified during the year based on review of stress / NPA performance and other factors.

The Bank’s current guidelines on due diligence with regard to obtaining satisfactory credit reports, undertaking visits, due diligence of suppliers /contractors etc., checking of CIBIL/Credit Information Companies [CICs] database for consumer/commercial credit information reports, CIBIL MSME Ranking [CMR] (wherever available), KYC and AML norms, checking of RBI defaulters list, and CRILC database, caution advices etc., guidelines on connected lending, multiple banking arrangements, NOC from existing lenders, etc., wherever applicable, shall be followed.

No additional facilities would be granted by the Bank to the wilful defaulters as identified by it and those appearing in the list as published/disseminated by RBI/CICs. In addition, such companies/entities (including their entrepreneurs / promoters) where the Bank has identified siphoning / diversion of funds, misrepresentation, falsification of accounts and fraudulent transactions would be debarred from the Bank’s exposurefor floating new ventures

[2] Projects in the service sector which do <u>not</u> create substantial tangible fixed assets and invest in light assets but generate comfortable cash flows.

for a period of 5 years from the date of removal of their name from the list of wilful defaulters.

2.4.3 **Fair Practices Code for lenders/ Code of commitment to Micro, Small and Medium Enterprises [MSMEs]:**

Fair Practices Code for Lenders, as per RBI guidelines, has been adopted by the Bank and hosted on Bank's website. The Code sets out the guidelines for processing of loan applications, appraisal, disbursement, post-disbursement supervision, etc. A Grievance Redressal Mechanism has also been put in place to resolve the disputes arising out of the Fair Practices Code. The Bank has adopted the Code of Commitment to Micro, Smalland Medium Enterprises (MSMEs) of Banking Codes and Standards Board of India [BCSBI].

BUSINESS POLICY OF VERTICALS

3 INSTITUTIONAL LENDING

3.1 *INTRODUCTION*

The institutional lending portfolio of the Bank consists predominantly of resource support / refinance to Scheduled Commercial Banks, Scheduled Cooperative Banks, Non Banking Financial Companies [NBFCs], Small Finance Banks [SFB] and to Primary Lending Institutions [PLIs], comprising State Financial Corporations [SFCs], State Industrial Development/ Investment Corporations [SIDCs / SIICs]. In addition, the portfolio also includes resource support/ term loan to Public Sector Undertakings benefiting the MSMEs.

3.2 *ASSISTANCE TO SCHEDULED COMMERCIAL BANKS*

The strategy adopted in FY 2018 to create long term assets under the scheme would continue to be the thrust area for FY 2019. Exposure to the scheduled commercial banks by way of refinance during FY 2019 would be encouraged but within the individual counterparty exposure limits fixed by the Bank.The individual bank-wise caps are fixed on the basis of category of the bank, its networth and risk rating.

3.3 *ASSISTANCE TO SCHEDULED CO-OPERATIVE BANKS & REGIONAL RURAL BANKS [RRBs]*

Over the years, Scheduled Co-operative Banks have registered significant growth in the number, size and volume of business handled. Some of the RRBs are also now profit driven and, in addition to commercial lending such as agriculture and MSMEs, these banks also compete with scheduled commercial banks for fee and commission, income from remittances, sale of insurance products and mutual fund schemes. Counterparty exposure limits to these banks shall be decided on a case to case basis, depending on risk rating and other factors such as networth of the bank, eligible MSE portfolio, overall financial health, compliance with regulatory directives, etc.

3.4 *ASSISTANCE TO NBFCs*

The NBFCs (both in the category of Deposit taking and Non Deposit taking) registered with RBI, which are engaged in financing MSMEs and in business for the last 5 years, are, prima facie, eligible for resource support from the Bank subject to meeting the prescribed BfS norms relating to capital adequacy ratio, gross NPA, net NPA, minimum investment grade external rating and compliance with all the prudential guidelines prescribed by RBI from time to time.

The Bank provides term loan / resource support to Asset Finance Companies. The assistance is also extended to Loan Companies, if the loan is given for income generating activities.

The assistance to NBFCs would be secured by, exclusive charge / first pari-passu charge with other lenders by way of hypothecation of book debts of the NBFC with suitable margin, collateral security etc.

Direct Assignment: Purchase of pool of MSME asset from NBFC will be considered on a case to case basis in accordance with Bank's internal norms and the extant RBI guidelines in this regard.

3.5 *ASSISTANCE TO SFBs*

Refinance from SIDBI, which is exempt from CRR / SLR requirements, is expected to be one of the major forms of support to SFBs in their initial years, particularly until they are able to build up a resource base from public deposits. As per the Scheme for Refinance to SFBs approved by the Board, counter party exposure to each individual SFB shall be capped based on its internal rating. The interest rates shall be finalized on a case to case basis based on relevant factors / prevailing market conditions at the time of sanction / drawal.

In addition to the above Scheme for Refinance to SFBs, subject to their meeting prescribed eligibility criteria, SFBs would also be considered for refinance under MSME Refinance Fund [as already permitted by RBI] / SIDBI's Refinance Scheme for Micro & Small Enterprises on terms and conditions as applicable for such refinance.

3.6 *ASSISTANCE TO STATE FINANCIAL CORPORATIONS [SFCs]*

In view of Banks decision to phase out SFCs portfolio, SFCs are not eligible for refinance under Line of Credit. However, refinance could be considered to SFCs upto 40% of the actual repayment subject to compliance of various performance parameters decided by Bank.

Given the sizeable exposure of the Bank to the SFCs, the performance of all the SFCs would continue to be closely monitored both by way of on-site and off-site mechanisms. Further, with a view to bringing about convergence in the regulatory framework, vis-à-vis the industry practices, the Bank has been advising the SFCs to comply with prudential norms prescribed by RBI.

3.7 *ASSISTANCE TO SIDCs/SIICs*

The Bank would continue to make a conscious attempt, as hitherto, to reduce / exit from the existing exposures to weaker SIDCs / SIICs (including TFIDCs).

4 LENDING UNDER SIDBI FOUNDATION FOR MICRO CREDIT [SFMC]

4.1 *INTRODUCTION*

The Micro Finance sector is on a growth path after its revival post AP crisis with regulator viz., RBI and the Self Regulatory Organizations (SROs), viz., MFIN / Sa-Dhan, ensuring a strong and clear regulatory framework for MFIs to operate efficiently. The guidelines also entailed the MFI lenders to assess the MFIs' performance in terms of sustainability as well as regulatory compliance. Flow of funds from banks to MFIs has risen substantially enabling the sector to register impressive growth. SIDBI, being a pioneer financial institution in the micro finance space, continued to provide financial assistance, in the form of equity, quasi-equity and term loans, etc., while advocating and implementing various responsible finance practices, viz., Code of Conduct Assessment (COCA), etc.

The microfinance industry in India has been a strong enabler in including the financially underserved and unserved in the formal financial ecosystem. The RBI constituted Mohanty Committee in its report (December 2015) on "Medium term Path on Financial Inclusion", recommended that bank credit to MFI's should be encouraged. However, the growth in the sector has also been accompanied by challenges such as increase in risks due to geographical concentration, socio-political risks and high churn in human capital employed by these institutions.

The demonetization in November 2016 hadjolted the industry. However, the impact of demonetization on the sector is expected to be positive with MFIs emerging stronger, adopting better risk management practices and bringing greater focus on cashless operations through digital channels.

With several leading MFIs reporting Portfolio at Risk (PAR) in excess of benchmark norms on account of deterioration in the asset quality, the large MFIs are expected to book losses on account of higher provisioning / write offs of bad debts. As many of these MFIs are expected to not able to meet benchmark norms of sanction relating to PAR / OSS, Bank would adopt a cautious approach during the current FY by laying emphasis on track record of capital infusion, compliance with regulatory guidelines, strict adherence to responsible lending practices and long-term sustainability in terms of financial and operational efficiencies.

Keeping in view Bank's long term experience in the microfinance sector, it is proposed to initiate a pilot to provide direct credit to the microfinance clients through a Partnership Arrangement [PA] model similar to BC model being operated by the commercial banks with the objective to facilitate availability of low cost funds to end beneficiaries under SFMC dispensation and to disrupt the market and make the micro finance loans cheaper across the board.

With the sector regaining confidence and momentum, the Bank has also adopted a 'growth strategy' approach for the Micro Credit business. It is proposed to continue the same strategy during FY 2019.

4.2 ***FOCUS***

On asset quality, focus would continue to be on risk management through the assessment, monitoring and exposure management. The Bank uses internal rating module for MFIs to bring objectivity in assessing / grading the risks of the loan proposals. Bank focuses on MFIs and NBFCs with good track record of resource mobilization, capital infusion, strong systems, compliances with regulatory guidelines, adherence to responsible lending practices and long term sustainability in terms of financial and operational efficiencies.

4.3 *PRODUCT PROFILE*

4.3.1 Support to MFIs and NBFC- MFIs

SFMC shall continue with term loan, subordinate debt, long tenor loans to MFIs for on-lending to micro enterprises and to service providers and to the Missing Middle segment. Bank's equity and related investments in MFIs will be guided by statutory guidelines.

4.3.2 India Microfinance Equity Fund (IMEF)

To provide equity and quasi equity support to smaller MFIs to help them maintain growth and achieve scale and efficiency in their operations, IMEF is operated by the Bank with funds from GoI. Under the Scheme, assistance in the form of sub-debt, Equity and quasi-equity is provided to smaller socially oriented MFIs, operating mostly in underserved / unserved areas of the Country. The focus on increasing the overall investments under the scheme to benefit large number of smaller MFIs would continue.

5 DIRECT LENDING TO MSMEs

5.1 *ASSISTANCE UNDER SIDBI MAKE IN INDIA SOFT LOAN FUND FOR MICRO, SMALL & MEDIUM ENTERPRISES [SMILE]*

The Central Government launched an ambitious 'Make in India' campaign in FY 2016 to make India a manufacturing hub and has identified 25 sectors under the 'Make in India' initiative. The Bank had launched "SIDBI Make in India Loan for Micro, Small & Medium Enterprises (SMILE) with a fund corpus of `10,000 croreto be met out of the Budget allocation. The objective of SMILE is to provide soft loan in the nature of quasi-equity and term loan on relatively soft terms to eligible new and existing MSMEs in India with endeavour to maximise utilisation of the fund.

5.2 *ASSISTANCE FOR SUSTAINABLE DEVELOPMENT*

The Bank has recognized sustainable development of the MSME sector as one of the high potential areas for strengthening the competitiveness of MSMEs in India. The Bank has been operating Lines of Credit from various multilateral/ bilateral agencies viz. Kreditanstalt fur Wiederaufbau (KfW), Germany, Japan International Cooperation Agency [JICA], Japan, AgenceFrancaise de Developpement[AfD], France, for financing energy efficient and cleaner environment investments in MSMEs with an objective to promoteuse of energy efficient and cleaner technologies, reduce CO_2 emissions, promote and sustain renewable energy, encourage technology innovation, upscale demonstration and commercialization of innovative technology based projects.

- International/Multilateral Lines of Credit for Sustainable Finance: Recognizing the importance of Energy Efficiency [EE] & Cleaner Production [CP] in tackling the challenge of climate change and curtailing the demand for energy from fossil fuels, SIDBI has been operating Lines of Credit from various multilateral/ bilateral agencies. These EE/CP investments will result in energy savings and reduction in global Green House Gas [GHG] emissions. Besides, it also strengthens the competitiveness of MSMEs in India and in global markets.
- The 4E (End-to-End Energy Efficiency) - Solutions and Financing schemes: The End to End Energy Efficiency Solutions [4E Solutions] launched by SIDBI provides technical support to its MSMEs to improve their energy savings by availing the services of Technical Consultant / ESCOs at a reasonable cost with assurance on the quality of services.
- Partial Risk Sharing Facility (PRSF) for Energy Efficiency Project:The Bank is the Project Executing Agency (PEA) for the World Bank Project, viz. “Partial Risk Sharing Facility for Energy Efficiency (PRSF)”. The objective of the project is to support the GoI efforts to transform the EE market in India by promoting increased level of EE investments, particularly through energy service performance contracting (ESPC) delivered through ESCOs.

  Under the project, SIDBI (PEA) provides partial risk coverage to the extent of 75% of the loans given by Banks / FIs / NBFCs (including SIDBI loans) to ESCOs and ESCO-implemented projects. Minimum loan size eligible for coverage under PRSF is `10 lakh and the maximum loan eligible for coverage is `15 crore per project.
- Assistance for Technology Innovation Projects **:** Need for developing national capabilities to innovate and create business opportunities in emerging technology areas has been acutely felt as there continues to be a dearth of early stage funding for commercialization of innovations by MSMEs due to higher risks of investment in unproven

technologies. The Bank has joined hands with Technology Information Forecasting and Assessment Council (TIFAC), Dept. of Science & Technology, GoI for implementing Technology Innovation Programme[SRIJAN Scheme].

5.3 *WORKING CAPITAL ASSISTANCE*

Working Capital Assistance would be considered selectively to:

- existing customers who are solely banking with the Bank ;
- existing customers of the Bank (who are also banking with other banks) and have placed major share of immovable security with the Bank;
- existing well performing entities who are new to the Bank and do not enjoy working capital facility with any other bank;
- New entities where term loan is considered by the Bank.

Takeover of working capital accounts, as a part of term loan takeover, may be considered subject to compliance of takeover guidelines.

5.4 *ASSISTANCE TO SERVICE SECTOR PROJECTS*

5.4.1 **Thrust Business Areas**

While the Bank would consider support to all eligible service sector activities, the following areas would be accorded due emphasis for faster asset growth during the year:

(i) Financing of trade and supply chain

(ii) Logistics & supply chain management

(iii) Organized retail outlets/ Retail Chains/dealerships

(iv) Restaurants/food chains/Quick Service Restaurants etc.

(v) Healthcare/Diagnostic Chains/Specialty Clinics etc.

(vi) Tourism related services

(vii) IT / IT enabled services

(viii) Franchisee chains of well known brands,

(ix) Warehouses

5.4.2 Approaches to finance Service Sector

The assistance to service sector is broadly divided into two categories viz. (a) asset backed term loan assistanceand (b) term loan assistance to asset light service sector enterprises.

Asset backed assistance to service sector enterprises - Asset backed term loan assistance would include assistance towards projects involving substantial primary and /or collateral security in the form of fixed assets like immovable properties and equipment, etc**.** Warehouses and hotels would generally fall under this category.

Term loan assistance to asset light service sector enterprises - Some of the projects in the service sector do not create tangible fixed assets and invest in light assets and, therefore, may not meet security related norms of asset backed assistance, but these are found to generate comfortable cash flows. These segments include IT and other knowledge based industries, restaurant chains, diagnostic/ specialty clinics etc. As there is good potential for considering assistance to these sectors, proposals of deserving customers could be considered for Bank's financial support based on merits.

5.5 *ASSISTANCE FOR RECEIVABLE FINANCE*

MSME Receivable Finance Scheme [MSME-RFS] is being operated by the Bank to mitigate the receivables problem of MSME sellers and improving their cash flow / liquidity.

RFS covers discounting/purchasing of bills/invoices arising out of sale of indigenous components/ parts/ sub-assemblies/ accessories/ intermediates manufactured/ job work done/ services provided by MSMEs and eligible service providers to Large Purchaser Corporates.

End-use of funds is verified by undertaking visits to select MSME beneficiary units and random verification of the purchased/discounted invoices/ bills to ensure utilization of funds as per objectives of the Scheme.

In order to improve the quality of overall portfolio, external rating is made mandatory under MSME RFS. Wherever possible, personal guarantees of directors would also be obtained for such facilities. More thrust is given for creating a portfolio of secured/partially secured limits and limits not backed by collateral security with external rating of 'AA(-)' and above. For existing customers, the thrust would be on retaining customers with a good track record.

To help existing customers, the entire credit purchases both from MSMEs and non-MSMEs, can be covered under Trade Finance Scheme/

Raw Material Assistance Scheme, after ensuring that there is no double financing. The scheme is also being extended to new customers with certain additional criteria.

5.6 *CO-LENDING WITH SFBs AND NBFCs*

NBFCs specialize in meeting the credit needs of niche areas such as hire purchase, financing of physical assets, commercial vehicles and infrastructure loans. They cater to a wide range of financial activities particularly in areas where commercial banks have limited penetration. Further, the NBFCs and SFBs are expected to play a main role in fostering inclusive growth, especially in sectors like MSMEs in the years to come. Accordingly, it is proposed to enter into Joint lending programme / arrangements with SFBs, NBFCs etc. for extending financial assistance in the form of term loans to MSMEs against a single common application for meeting their capital expenditure requirements.

6 CREDIT RISK MANAGEMENT

In terms of RBI guidelines the banks should have a robust Credit Risk Management (CRM) system which is sensitive and responsive to the credit risks emanating from its dealings with individuals, corporates, banks, FIs or sovereign. According to the guidelines, banks have to devise a risk management framework oriented towards their requirements, dictated by size, complexity of business, risk philosophy, marketing perception, etc.

The dimensions of credit risk to which the Bank is exposed to fundamentally emanate from exposure to MSME enterprises/ sector which are characterized by weaknesses in corporate structure, systems, accounting standards, lack of availability/ reliability of information and vulnerability to external developments, risk concentration in exposure to the MSME sector.

6.1 ***CREDIT RISK STRATEGY***

In line with the strategy for managing risks in the credit portfolio, following tenets have been incorporated in the Loan Policy:

(a)Monitoring exposure to SFCs/ SIDCs as a percentage of total portfolios.

(b)Use of internal rating models to measure credit risk for majority of the customer categories.

(c)Risk control, *inter alia*, through implementation of exposure limit framework for different segments of customers.

(d)Implementation of processes to ensure that initiative to increase lending by innovation in products, target clients, etc., does not lead to deterioration of the asset quality of the Bank's portfolio.

(e)Installation of an enabling framework capable of grading the risk and eventually linking pricing to internal ratings as suited to the Bank's requirements.

6.2 RISK MEASUREMENT

6.2.1 **Internal Credit Rating Systems -** The Bank usesCredit Appraisal and Rating Tool [CART] to processloan proposals [Greenfield and existing units]and rating of loan proposals received from existing units fulfilling certain criteria.

For loans outside the purview of rating in CART, Risk Assessment Models [RAMs]arebeing used.

6.2.2 **Investment Grades -** Proposals with internal obligor risk rating at the time of appraisal between S1 to S8 in RAM [equivalent grade in CART] are considered as 'investment grade' i.e. suitable for extending credit facility. However, in respect of certain sectors, higher investment grade ratings have been stipulatedfor greater selectivity and credit quality as indicated in **Annexure – II** with minimum internal rating grade and compliance of other conditions specified. Changes to this list may be made from time to time based on internal review.

6.3 RISK MITIGATION

The present credit risk mitigation strategies in vogue would be continued which are primarily being applied at two levels. At the project specific level [transaction level], efforts are made to identify critical risk factors and suitable mitigation measures are explored and stipulated, wherever possible. Risk rating would be used for objective grading of risk. At the portfolio level, the Bank has been following a strategy of exposure management and prudential caps on credit exposures under various activity/ industry /type of customer.

Further, all credit proposals for assistance from the Bank and renewal or enhancement of fund / non-fund based limits with aggregate exposure above `500 lakh will be considered with applicable External Rating (Bank Loan Rating) by an RBI accredited credit rating agencies. Risk concerns indicated therein should be specifically commented upon in the Appraisal Memorandum.

6.4 ***EXTERNAL RATINGS***

In respect of MSME-RFS limits and resource support to NBFCs &MFIs, external rating (Long term rating) by RBI accredited rating agencies is considered for the purpose of eligibility and pricing with minimum specified external rating grade.

6.5 ***PRICING***

In the existing scenario of dynamic interest rates, competition and the need for the Bank to expand the direct finance portfolio with addition of quality assets, a dynamic pricing strategy has become *sine qua non*. The pricing of loans is carried out as per the gradation of risk determined by the internal ratings for various customer segments. With a view to remaining competitive in the market, the existing practice of fixing the interest/ discount rate depending upon competitiveness/ demand, asset cover and such other factors, may continue. As regards assistance sanctioned to infrastructure projects and such other projects under joint finance/ consortium arrangement, the interest rate stipulated by the lead institution/ other banks would normally be followed.

In case of projects involving multiple/joint/consortium financing, interest rate reset clauses would be in line with the practice obtaining with other banks/ institutions.

6.6 ***RISK CATEGORISATION OF CUSTOMERS FROM AML PERSPECTIVE***

In compliance with the Policy Guidelines on KYC Norms and Anti Money Laundering [AML] Standards, the process of risk categorization of customers has been put in place depending upon their activity, location, constitution, etc.

6.7 ***MANAGEMENT OF ASSETCONCENTRATION***

6.7.1 **Exposure Caps and Counterparty/Activity/Industry exposure**

Asset concentration is being managed by the Bank by way of various exposure caps/ norms for credit deployment which have been fixed, as under, taking into account the norms prescribed by RBI.Exposure cap has beend defined for SIDBI on solo basis (as a % of capital funds of the Bank) and SIDBI group-wide (as a % of capital funds of the group).

Such internal caps have been laid down in respect of different schemes of direct assistance and for various industrial sectors as summarized in the table at Annexure – III. The exposure caps are applicable on exposure taken from the banking book as well as Treasury.

6.7.2 **Policy on Group Lending**

The Bank considers assistance to large groups only under select schemes such as MSME-RFS, NBFC and Infrastructure Scheme. Decisions on sanction/ continuation of exposure on a concern whose group/ associate concern(s) has defaulted to the Bank and / or to other banks/ FIs are being taken on case specific merits. The practice would be continued and a final view on such cases would be taken by the delegated sanctioning authorities.

Further, SIDBI Group wide Exposure cap has also been defined in all the above scenarios.

6.7.3 **Restricted industries**

The extant instructions for a cautious approach in respect of industries such as chemical dyes & dye intermediates, industrial oxygen, distilleries, etc., would continue**.** Assistance to deserving units in the list could be considered if they have an internal obligor risk rating of S7 or above. Industries consuming / producing ozone depleting substances viz. Chlorofluorocarbons [CFCs], Halon, Carbon tetrachloride, Methyl chloroform, Hydrobromo-fluorocarbons [HBFCs), hydrochloro-fluorocarbons [HCFCs], Methyl bromide, Bromochloromethane (BCM), etc., would **not** be assisted at all.

7 CONCLUSION

Efficient credit delivery is the key to quality portfolio build up and customer retention. The Loan Policy gives adequate flexibility to develop viable business proposals. The Policy has also put in place a suitable structure for approval / clearance of new products. Hence, any business proposition considered to be viable and bankable should not be lost on account of non-availability of a suitable scheme/product. It will also be the endeavor of the Bank to further simplify and streamline procedures/processes to expedite the credit delivery besides making efficient use of IT for internal credit monitoring.

Annexure - I

Benchmarks for Sanction (BfS)

A. Term Loan

Sl. No.	Parameters	BfS Norm	Relaxation Cap
1	Prudential Rating	S8	No relaxation
2	Debt-equity Ratio (DER)[3]	3:1[4]	3 : 1
3	Promoters' contribution[5]		
	New entity[6]	33%	25%
	Existing entity[7]	25%	20%
4	Projected DSCR[8]	1.50	1.25
5	Fixed asset coverage Ratio (FACR)		
	New entity	1.00	0.90[9]
	Existing entity		
	Asset light & Cash-flow based	0.50	0.40
6	Asset coverage Ratio (ACR)		
	New entity	1.40	1.30
	Existing entity	1.30	1.20
	Asset light & Cash-flow based	1.30	1.00

B. Working Capital

Sl. No.	Parameters	BfS Norm	Relaxation Cap
1	Prudential Rating	S8	No relaxation
2	Interest coverage ratio (ICR)[10]		
	New entity	1.50	1.50
	Existing entity[11]	1.25	1.10
3	Fixed asset coverage Ratio (FACR)		
	New entity	0.75	0.75
	Existing entity		0.65
4	Asset coverage Ratio (ACR)		
	New entity	1.40	1.30
	Existing entity	1.30	1.20
5	Current ratio		
	New entity	1.25	1.10
	Existing entity	1.25	0.90

[3]For the company/entity as a whole after considering sub-debt [SD] and interest-free unsecured loans [IFUSL] as quasi equity
[4]4:1 for Fleets/Vehicles under logistics (Service Sector)
[5](a) Not applicable for secured business loan (SBL) & privileged customer scheme (PCS)**and** (b) 15% for proposals under SMILE
[6]A "New entity" is an entity newly set up/proposed to be set up. This would also include entities established in the past but with nil/ insignificant commercial production.
[7]An "Existing entity" is one which has already been established and is engaged in commercial production (with or without SIDBI's financial assistance)for minimum one year and audited accounts [for a full year] thereof are available.
[8]1.25 for service sector with no relaxation
[9]Applicable for customers having top 2 valid SME Credit rating/Bank loan rating of BBB+& above
[10] ICR = Earnings Before Deprecation, Interest and Tax [EDBIT] / Interest expenses
[11]Based on last audited accounts

Sl. No.	Parameters	BfS Norm	Relaxation Cap
6	TOL to TNW ratio		
	New entity	4:1	5:1
	Existing entity	4:1	6:1
7	Margin on stocks of raw materials, receivables/book debts etc.		
	New entity	30%	25%
	Existing entity	30%	20%

C. MSME – Receivable Finance

Sl. No.	Parameters	Secured (for renewal of existing limits)		Clean/ not backed by collateral	
		BfS Norm	Relaxation Cap	BfS Norm	Relaxation Cap
1	Prudential Rating	S8	No	AA-	No relaxation
2	Fixed asset coverage Ratio (FACR) [12]	0.75	0.65	Not applicable	
3	Asset coverage Ratio (ACR)[13]	1.25	1.10	Not applicable	
4	Current ratio				
	New customer	-	-	1.25	1.10
	Existing customer	1.25	0.85		0.90
5	Quick Ratio	0.50	0.40	0.50	0.40
6	TOL to TNW ratio				
	New customer	-	-	4:1	5:1
	Existing customer	4:1	6:1		6:1

D. Resource support to NBFCs [AFCs and Loan companies]

Sl. No.	Parameters[14]	BfS Norm	Relaxation Cap
1	Prudential Rating	S7 / A- and above	No relaxation
2	CRAR	>or =15%	>or =15%
3	Gross NPA	<10% for AAA	<10% for AAA
		<8% for AA	<8% for AA
		=< 6% for A	=< 6% for A
4	Net NPA	=<5% for AAA	=<5% for AAA
		=<4% for AA	=<4% for AA
		=<3% for A	=<3% for A

E. Small Finance Banks – Refinane to SFBs

Sl. No.	Parameters	BfS Norm	Relaxation Cap
1	Networth	> Or = ₹100 crore	> Or = ₹100 crore
2	CRAR	> Or = 15%	> Or = 15%
3	Gross NPA	< Or = 7 %	< Or = 7 %

[12] Not applicable in respect of proposals backed by LC / BG / Co-accpetance / 100% FD
[13] 1.00 for exposure backed by LC/ BG / Co-acceptance / 100% FD
[14] Unless specified otherwise, credit ratings A, AA or AAA would include respective (-) & (+) ratings.

F. Micro Credit – Resource support to MFIs

Sl. No.	Parameters	BfS Norm	Relaxation Cap
1	Prudential Rating	MfR5	No relaxation
2	Debt-equity ratio (DER)	10:1[15]	10 : 1
3	CRAR[16]	>or =15%	>or =15%
4	Portfolio at Risk >90 days	<5%	<7%
5	Operational self sufficiency (OSS)	100%	90%

Note:

a. TheProduct Verticals would align their scheme norms / operational guidelines with the Loan Policy framework.

b. Relaxation of BfS norms within the cap may be considered for maximum **3 [three]** parameters. Additional risk premium, if any, to be charged for such relaxations, will be decided by the delegated authority.

c. In respect of renewals at current level or reduced level, the delegated authority may relax the BfS norms suitably provided proper risk mitigants are put in place. The exit strategy, if any, would be decided by the delegated authority.

[15] 15:1 for Section 8 companies and Societies/Trusts

[16] Applicable for NBFC-MFIs

Annexure –II

Higher investment grade ratings – Select Sectors

Sr. No.	Particulars of industry	Minimum obligor rating
1	Iron & steel industry	S7
2	Textiles[a]	S7
3	Drugs & Pharmaceuticals	S7
4	Hotels[b]	S6
5	Hospitals[c]	S6
6	Food & Food Products	S7
7	Leather & Leather Products	S7
8	Power sector projects	S6
9	Wind Mill/ Solar Projects[d]	S7
10	Deserving units in the restricted list of Industries such as Chemical dyes & dye intermediates, industrial oxygen, distilleries etc.	S7

a) Except knitting cluster at Tirupur.

b) Hotel projects may be considered with matching collateral outside the project. Since Hotel projects typically have a relatively higher implementation/ stabilization period, a sufficiently long repayment period with ballooning/ stepped-up schedule may be drawn with sufficient moratorium.

Exemption for the norm regarding matching collateral outside the project may be considered for existing borrowers, subject to the following:

- The proposal meets eligibility criteria under PCS which is presently -
  - Two years satisfactory payment track record as per RiMV guidelines with at least one year principal repayment
  - Should have earned net profit in last two years of operation
  - Should not be in default to any bank/ FI.
  - The unit should not be in the caution list/ restricted list of industries specified in the Loan Policy/ intimated by HO from time to time.
- IACR for the project is 2.5;
- Extant guidelines of Valuation Policy may be adhered to. Further, valuation may be carried out afresh if no valuation is carried out through the centralized valuation process.

c) Hospital projects may be considered with matching collateral outside the project.Snce Hospital projects typically have a relatively higher implementation/ stabilization period, a sufficiently long repayment period with ballooning/ stepped-up schedule may be drawn with sufficient moratorium.

d) Wind Mill/ Solar Projects may not be considered on standalone basis. However, such projects for captive use (>50% of installed capacity) may be supported subject to existing cash flows of the borrowing entity being adequate to service the proposed debt obligation and the proposed exposure being secured with collateral in the form of immovable property/ liquid security having value of 50% of exposure.

Annexure - III

Exposure Caps

S. No.	Activity/ Industry		Exposure cap for SIDBI on solo basis (as a % of capital funds of the Bank)	SIDBI Group wide[17] Exposure cap (as a % of capital funds of the Group)
1	**Individual/ Borrower Group Exposure[18]**			
(a)	Direct assistance to MSMEs & specialized organizations marketing MSME products			
(i)	Single borrower		1%	1%
(ii)	Proprietorship entities		`10 crore	`10 crore
(iii)	Borrower Group exposure		3%	3%
(b)	NBFCs & private sector corporations			
(i)	Single borrower	Asset Finance Companies (AFCs)	15%	15%
		Others	10%	10%
(ii)	Borrower Group exposure		40%	40%
(c)	MSME Receivable Finance Scheme (MSME-RFS), direct resource support & such other form of bulk lending (except refinance and BRS) to public financial institutions, public sector undertakings and corporates			
(i)	Single borrower		15%	15%
(ii)	Borrower Group exposure		25%	25%
(d)	MFIs			
(i)	Single borrower	NBFC-MFIs	10%	10%
		other MFIs	3%	3%
(ii)	Borrower Group exposure	NBFC-MFIs	15%	15%
		other MFIs	5%	5%
2	MSME-RFS without collateral		30%	-
3	**Infrastructure activities/ projects**			
(a)	Total portfolio[19]		10%	10%

[17]Includes exposure from SIDBI, MUDRA Ltd., SVCL and STCL (wholly owned subsidiaries of the Bank)

[18]Exposure has been defined as under:

Product	Exposure computation
Fund based & Non-fund based facilities	Limit sanctioned or outstanding whichever is higher.

[19]Includes exposure to activities in various sub-sectors under infrastructure

Sr. No.	Activity/ Industry	Exposure cap for SIDBI on solo basis (as a % of capital funds of the Bank)	SIDBI Group wide Exposure cap (as a % of capital funds of the Group)
(b)	Power sector including generation, transmission and distribution.	5 %	5 %
4	***NBFCs***		
(a)	Exposure cap: BBB and BBB- rated	`100 crore	`100 crore
(b)	Exposure cap: NBFC-MFIs	30 %	30 %
(c)	Overall Exposure cap	200 %	200 %
5	***Contribution to Venture Capital Funds***[20]	40 %	40 %
6	***Resource Support***[21]	50 %	50 %
7	Exposure cap in service sector projects	40 %	40 %
8	***Industry Exposure***		
(a)	Cap on exposure to a particular industry other than those at (b) below	10 %	10 %
(b)			
(i)	Transport Equipment (including Auto and auto components)	30 %	30 %
(ii)	Textiles/ readymade garments and hosiery	30 %	30 %
(iii)	Engineering industry	30 %	30 %
(iv)	Electronics and electrical products	30 %	30 %
(v)	Agro based industries	30 %	30 %
9	***Direct Assignment business***	10 %	10 %
10	***Ceiling on Exposure in unsecured advances [including MSME-RFS without collateral at 2 above]***	100%	100%
11	***Individual bank/ institution wise limit***		
	Refinance/ Co-accepted Bills/ BRS/ LOCFC/ Resource Support [per institution]		
(a)	State Bank of India and Nationalized Banks	Individual banks/ FI wise limit as approved by the Board	
(b)	Private sector banks/ foreign banks		
(c)	SFCs [per institution]	15%	-
(d)	SIDCs including TFIDCs [per institution]	1%	-
(e)	SSIDCs [per institution]	0.5%	-
(f)	Scheduled Co-operative banks	5%	5%
(g)	Non scheduled Co-operative banks	-	`10 crore
(h)	Regional Rural Banks [per institution]	2.5%	2.5%
(i)	Small Finance Banks	15%	15%
11	***Aggregate exposure to***		
(a)	All SFCs (Aggregate)	`2000 crore	-
(b)	All SIDCs including TFIDCs (Aggregate)	5%	-
(c)	State Bank of India and all Nationalized Banks (aggregate)	500%	500%

[20] Subject to compliance with capital market exposure limit
[21] Excluding NBFCs

S. No.	***Activity/ Industry***	***Exposure cap for SIDBI on solo basis (as a % of capital funds of the Bank)***	***SIDBI Group wide Exposure cap (as a % of capital funds of the Group)***
(d)	*All FIs (aggregate)*[22]	*100%*	*100%*
(e)	*Private Sector Banks (aggregate)*	*700%*	*700%*
(f)	*Foreign Banks (aggregate)*	*100%*	*100%*
(g)	*Scheduled Co-operative banks (aggregate)*	*10%*	*10%*
(h)	*Non scheduled Co-operative banks*	*-*	*`100 crore*
(i)	*Regional Rural Banks (aggregate)*	*5%*	*20%*
(j)	*Small Finance Banks (aggregate)*	*40%*	*60%*
12	*Intra Group Exposure*	*10% of paid up capital and reserves in case of regulated financial services company.*	
		20% of paid up capital and reserves in case of the group i.e. all group entities (financial and non financial) taken together.	

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[22] Excluding SFCs and SIDCs