

INDIAN OVERSEAS BANK
SME DEPARTMENT
CENTRAL OFFICE

LOAN POLICY FOR MSE SECTOR

BACKGROUND

Micro and Small Enterprises plays vital role in the economic well being of the country due to their ability to generate employment, foster entrepreneurship. They provide depth to the industrial and commercial base of the economy. They also contribute in significant measure to the GDP and exports from the country.

Government of India, is attaching great importance to this sector and taking various policy measures to enhance the flow of credit to MSME sector. To ensure systematic and smooth growth of the MSME sector, the Government of India enacted the Micro, Small and Medium Enterprises Development Act 2006 (MSMED Act 2006) on 16.06.2006, which came into effect from 02.10.2006. The act replaced the concept of tiny/small scale industries sector with the expanded Micro, Small and Medium Enterprises Sector which includes Micro, Small and Medium manufacturing as well as service enterprises.

The problems of the MSE sector are multifarious and credit related issues are diverse, which call for multi-pronged, integrated, and balanced approach on the part of the bank. Hence it is necessary to have a comprehensive liberal and forward looking policy on funding of MSE enterprises.

To address the problems faced by the MSME sector, RBI had constituted a working group under the chairmanship of Dr.K.C. Chakrabarty to suggest measures for Rehabilitation of sick MSME units and for improving the flow of credit to MSME sector. The working Group, in their report, has given various recommendations and suggested measures to be adopted by banks, Government and other Agencies. RBI advised all Banks to formulate a loan policy governing the extension of credit to MSE sector in the light of recommendations of the working group and BCSBI 's code of commitment to Micro and Small Enterprises.

Accordingly, a Loan policy for MSE sector was framed and approved by the Board and the same is placed in our Website. There has been no significant changes in the Loan Policy in MSE sector since framing the first policy on . But in the light of recent revision by RBI in classification

criteria under Micro and Small Enterprises which are categorized under Priority Sector, it is felt that the policy be updated and modified and be placed to the Board for approval.

LOAN POLICY FOR MSME SECTOR

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I. PREAMBLE

Micro and Small Enterprises (MSEs) are considered as the growth engines of the Indian economy due to their spread and depth. They create vast employment opportunities and contribute significantly to our GDP. Their share in the exports is also significant. The scope of lending to Micro and Small Enterprises is expanding due to various policy measures of banks, RBI and Government of India. A comprehensive and liberal lending policy is required to enable the MSE sector to play its pre eminent role on the Indian economy without any hurdles. Accordingly, this policy is fine tuned to meet the genuine requirements and aspirations of the MSE sector.

II. OBJECTIVES OF THE POLICY

The percentage of our Bank's MSE credit to total domestic credit stood at 13.03 as on 31.03.2012. The prime objective of the earlier policy was to improve the percentage of MSE credit to domestic credit 12% by 31.03.2012 from 11.48% as on 31.03.2011. The objective has since been achieved with our MSE credit touching 13.03 as on 31.03.2012 on the Gross Domestic Credit for MSE credit. Through this policy, we place our objective at 20% of the gross Domestic Credit by 30.03.2015 thereby facilitating smooth flow of credit to MSE sector. The other objectives of the policy are as under:

1. To describe the MSE sector and its functional coverage.
2. To lay down guidelines for assessment of credit to MSE units.
3. To make available adequate and hassle-free credit facilities to MSE enterprises
4. To achieve various growth parameters prescribed for MSE sector
4. To comply with RBI/Government of India guidelines and instructions on MSE financing.
5. To give more thrust to Micro and Small Enterprises
6. To adopt cluster based financing for Micro and Small Enterprises
7. To improve coverage under Credit Guarantee Scheme of CGTMSE.
8. To implement various Government sponsored schemes applicable to MSE sector.
9. To adhere to the BCSBI's Code of Commitment to Micro and Small Enterprises.
10. To describe the growth plan for this sector by establishing SME Processing Centres at various regions and improve the turn around time for sanction of MSME proposals.

III. DEFINITION OF MSE ENTERPRISES.

In order to facilitate the promotion and development of Micro, Small and Medium Enterprises, the Government of India enacted THE MICRO, SMALL AND MEDIUM ENTERPRISES DEVELOPMENT ACT 2006. (MSMED ACT 2006) The Act became operational from 02.10.2006. The Act introduces the concept of "Enterprises" as against the "Industries".

The Enterprises are now grouped under two major heads namely manufacturing and services. The MSMED Act 2006 defines various categories of enterprises in terms of Investment in Plant, Machinery and Equipments. Various categories of Micro and Small Enterprises are defined as under:

MICRO AND SMALL ENTERPRISES:

A. DIRECT FINANCE

The limits for investment in plant and machinery /equipment for manufacturing / service enterprise, as notified by Ministry of Micro Small and Medium Enterprises, vide S.O.1642(E) dated 09.09,2006 are as under:

Manufacturing Sector	
Enterprises	Investment in Plant and Machinery
Micro Enterprises	Do not exceed twenty five lakh rupees
Small Enterprises	More than twenty five lakh rupees but does not exceed five crore rupees
Service Sector - Loans upto Rs.1 Crore	
Enterprises	Investment in equipment
Micro Enterprises	Does not exceed ten lakh rupees
Small Enterprises	More than ten lakh rupees but does not exceed two crore rupees

Bank loans to micro and small enterprises both manufacturing and service are eligible to be classified under priority sector as per the following:

Manufacturing Enterprises

The Micro and Small enterprises engaged in the manufacture or production of goods to any industry specified in the first schedule to the Industries (Development and regulation) Act, 1951. The manufacturing enterprises are defined in terms of investment in plant and machinery.

Loans for food and agro processing

Loans for food and agro processing will be classified under Micro and Small Enterprises, provided the units satisfy investments criteria prescribed for Micro and Small Enterprises, as provided in MSMED Act, 2006.

Service Enterprises

Bank loans upto Rs. 2 Crores per unit to Micro and Small Enterprises engaged in providing or rendering of services and defined in terms of investment in equipment under MSMED Act, 2006.

Export credit to MSE units (both manufacturing and services) for exporting of goods/ services produced by them.

KHADI AND VILLAGE INDUSTRIES SECTOR (KVI)

All loans sanctioned to units in the KVI sector, irrespective of their size of operations, location and amount of original investment in plant and machinery. Such loans will be eligible for classification under the sub target of 60 percent prescribed for micro enterprises within the micro and small enterprises segment under priority sector.

B. INDIRECT FINANCE TO MSE SECTOR

- (i) Loans to persons involved in assisting the decentralised sector in the supply of inputs to and marketing of outputs of artisans village and cottage industries.
- (ii) Loans to cooperatives of producers in the decentralised sector viz., artisans village and cottage industries
- (iii) Loans sanctioned by banks to MFIs for on lending to MSE sector as per the conditions specified in paragraph VIII of this circular (RBI Circular)

IV. SCOPE AND COVERAGE

This policy covers credit facilities to micro and small enterprises. (both manufacturing and services sector) and all related issues such as assessment of credit, margin norms, security requirements, coverage under Credit Guarantee Scheme etc.,

V. GUIDELINES ON MSE FINANCE

Advances to MSE sector will be assessed like any other advance (except for the specific relaxations and concessions given in this policy) and credit decisions will be taken based on viability, merits and commercial judgment in each case as per general norms of lending. The credit appraisal will be made in a transparent and non-discriminatory manner. All genuine and just requirements of the MSE units will be considered and adequate amount of credit will be sanctioned to ensure that the unit does not suffer for want of funds at a later date.

Necessary credit support will be extended to MSE units for business restructuring, modernization, expansion, diversification and technological up gradation as may be required from time to time.

The following type of credit facilities will be extended to MSE units.

1. Term Loans
2. Project Finance
3. Working Capital Finance
4. Purchase and discounting of Bills
5. Negotiation of Bills
6. Non fund based facilities such as LC and LG
7. Pre shipment/Post shipment finance
8. Credit facilities under Bank's special credit schemes such as Sanjeevani, Easy Trade Finance, Commercial Cash Credit against Jewellery etc.,
9. Any other type of credit depending on specific need.
10. Line of credit in specific cases as per requirement.

ASSESSMENT OF CREDIT FOR MSE UNITS

- a. Simplified procedures will be adopted for sanction of working capital limits. 20% of the projected and accepted annual turnover will be extended as working capital limit to MSE units requiring aggregate fund based working capital limits up to Rs.7.5 crore. Borrower has to bring in 5% of the accepted turnover as margin. Current Ratio of 1.25 will be acceptable in such cases.

- b. For MSE units requiring working capital limits above Rs.7.5 crore and up to Rs.10 crore, the Maximum Permissible Bank Finance (MPBF) method based on Credit Monitoring Arrangement (CMA) data will be followed.
- c. For MSE units requiring working capital limits over Rs.10 crore, Cash budget system or MPBF method, at the option of the borrower, will continue to be followed.
- d. A combined working capital limit will be allowed against the stock and receivables without any sub limit for CC against receivables. However, different margins may be fixed for stock and receivables.
- e. Lending will be based on scoring model for advances upto Rs.2 crores. Information required for scoring model will be incorporated in the application form itself. No individual risk rating is required in such cases.
- f. If the bank sanction term loan solely or jointly with one or more Banks, working capital limit will also be sanctioned solely or jointly (in the ratio of term loan) to avoid delay in commencement of commercial production. It will also be ensured that there are no cases where term loan has been sanctioned but sanction of working capital facilities is awaited.
- g. The interest payable up to six months after commercial production may be included as part of the project cost for assessment of credit requirements. Sufficient moratorium period say, upto six months, after commencement of commercial production, may be allowed for repayment of principal amount wherever required, to enable the unit establish itself in the market.
- h. When the sanctioning authority decides to reject a MSE credit application, the same will be conveyed to the applicant only after obtaining approval from the next higher authority.

1 MARGIN NORMS

- I. No margin is required for loans upto Rs.50000/-
- II. Minimum margin requirements for loans/credit facilities above Rs.50000/- are as under:

A. TERM LOANS

1. For loans above Rs.50000/- and up to Rs.5 Lac -10%
2. For loans above Rs.5 Lac -15%
3. In case of Term Loans for acquiring second hand machineries, higher margin may be stipulated on case-to-case basis.

d. Even when the loan is eligible to be covered under the Guarantee cover of CGTMSE, if the borrower prefers to bring acceptable collateral security and third party guarantee, in lieu of the CGTMSE Guarantee Cover, the same will be considered, after obtaining a letter from the applicant stating that he is offering collateral of his own volition and he is aware of the credit guarantee available for his credit facilities.

All collateral free loans above Rs.10 lacs and upto Rs.100 lacs will be brought under cover of Credit Guarantee Scheme of CGTMSE.

2. As per General Loan Policy Document secured advances can be sanctioned by Branch Managers upto the level of Scale IV only by taking collateral securities to a minimum extent of 75% of the credit limits sanctioned. This will be relaxed in respect of MSE advance and Branch Managers upto the level of Scale IV will be allowed to sanction secured advances to MSE sector by taking collateral securities to a minimum extent of 60% of the credit limits sanctioned. Such sanctions should be supported by sound reasoning.
3. All branch Managers can sanction collateral free loans to MSE sector with CGTMSE Guarantee cover upto their per borrower limits subject to overall ceiling in force under the guarantee scheme.

CLUSTER BASED APPROACH

Clusters are defined as sectoral and geographical concentration of MSME units sharing common opportunities and threat. Thrust will be given to cluster based finance wherever recognized clusters are existing.

Following benefits of cluster based approach to lending will be taken advantage of:

- dealing with well defined groups
- availability of appropriate information for risk assessment and
- easy monitoring of borrowal units.

Diverse needs of the MSE units functioning within the cluster will be considered and adequate finance will be extended to such units .

Creation of infra structure facilities and establishment of common facility centres in clusters will also be financed in association with Central and State Government Agencies .

For limits upto Rs.2 lacs	Within 2 weeks
For limits above Rs.2 lacs and upto Rs.5 lacs	Within 4 weeks
For limits above Rs.5 lacs	Within a reasonable frame of time

Above time frame shall apply to disposal of applications for credit enhancement also.

A list of SIDBI identified cluster in association with UNIDO is provided in the Annexure.

PRICING AND CREDIT RATING OF MSE ADVANCES

As per Risk Management Policy of the Bank, all borrowal accounts with credit limits of Rs.1 crore and above to Large Corporates, Traders, SME and Infrastructure (Road and Power) must be rated under Risk Assessment Model (RAM) before sanction. Pricing of all loan facilities of Rs.1 crore and above is to be made based on the rating obtained.

A relaxation will be made for MSE borrowal accounts in this regard and MSE accounts for credit facilities upto Rs.2 crores need not be rated under RAM. Pricing of MSE credit facility upto Rs. 2 crores will be based on internal scoring model.

Bank will continue to prescribe separate and favourable interest rates for MSE credit in order to encourage the MSE sector.

DELAYED PAYMENTS TO MSME UNITS

As a measure to assist the MSE units to get the payment from large corporates without delay, suitable sub-limits will be fixed within the overall working capital limits sanctioned to large borrowers (borrowers enjoying working capital limits of Rs.10 crores and above from the banking system) specifically for meeting the payment obligations to MSE enterprises (and Medium Enterprises) for goods supplied or services rendered.

VI. CREDIT GUARANTEE TRUST FOR MICRO AND SMALL ENTERPRISES (CGTMSE)

Bank will encourage financing viable micro and small enterprises for fund based and non fund based limits upto Rs.100 lacs without collateral security or third party guarantee by taking advantage of the Credit Guarantee Scheme of CGTMSE.

Separate targets will be given to each branch for lending under Credit Guarantee Scheme of CGTMSE to improve our banks coverage under the scheme.

One time guarantee fee paid by MSE borrowers covered under the Credit Guarantee Scheme of CGTMSE upto credit limit of Rs.10 lacs will be reimbursed by the Bank after a period of 5 years or on the date of closure of a performing loan whichever is earlier.

VII.GROWTH PARAMETRES

The bank will set targets for growth of MSE credit by a minimum year on year growth of 20% or as mandated by Government of India from time to time. Targets will also be fixed each year for fresh disbursements of MSE credit. Currently the YoY growth in number of fresh borrowal accounts under Micro sector should be minimum of 10%. Within the MSE sector, thrust will be given to improve advances to Micro Enterprises . Efforts will be made to ensure that all sub sectors under MSE sector revised credit as under which is mandatory as per extant guidelines of RBI.

Micro Level I	40% of total credit to Micro and Small Enterprises
Micro Level II	20% of total credit to Micro and Small Enterprises
Small Enterprises	40% of total credit to Micro and Small Enterprises

VIII. STRATEGIES

To improve the flow of credit to MSE sector and to achieve the various targets and commitment for the MSE sector, the bank will adopt the following strategies:

- ❖ Branch Managers and other officials handling MSE credit will be imparted training to enable them to properly understand the nuances of MSE finance and opportunities in the sector. Efforts will be made to inculcate positive mindset amongst the officers towards financing MSE units.
- ❖ MSE credit processing centres will be set up at key locations to ensure prompt and efficient processing for all MSE credit applications.
- ❖ Simplified loan application forms in bilingual formats will be made available for loans to Micro Enterprises.

- ❖ Regionwise and branchwise targets will be fixed for lending to MSE sector and monthly review notes on Regionwise performance will be placed to Top Management.
- ❖ A separate target will be fixed to branches for sanction of loans under CGTMSE cover in order to increase the coverage under Credit Guarantee Scheme of CGTMSE.
- ❖ Thrust will be given to cluster based financing.
- ❖ SME branches and specialized SME branches will be opened at potential centres , identified clusters and industrial estates to enhance the flow of credit to MSE sector.
- ❖ At corporate level, bank will enter into MOU/tie up arrangement with the corporates and other agencies IN ALL SECTORS to formulate specific schemes for delivery of credit to MSE sector.
- ❖ Latest technology will be adopted for on line submission of MSE credit applications, tracking of applications and for MIS requirements.
- ❖ New credit products will be developed for MSE sector to meet the emerging requirements of the sector from time to time.
- ❖ Bank will implement all Government of India/State Government sponsored schemes for MSE sector and disburse credit under such schemes.
- ❖ Bank will avail refinance from SIDBI to augment the resources for lending to MSE sector, whenever considered necessary.

IX. MSME CARE CENTRES

MSME Care Centres which are now functioning at all our Regional Offices will be strengthened further to handle the grievances of Micro and Small Enterprises and also to guide the MSE Entrepreneurs.

X. FOLLOW UP OF MSE CREDIT

MSE loan portfolio will be monitored at branch and controlling office levels on regular basis. Warning signal with regard to irregularities in the accounts will be picked up promptly and probed into. Corrective measures will be initiated without loss of time to avoid the accounts slipping into sub standard category. Borrowal accounts will be restructured, wherever necessary, under the provisions of debt restructuring mechanism for SME enterprises.

A separate exit policy for sick non viable units has been framed duly approved by the Board.

If any accounts becomes sick, inspite of close monitoring and follow up action, such accounts will be dealt with sympathetically and shall be rehabilitated under bank's policy on nursing and rehabilitation of sick SME units, if they are potentially viable.

XI. CODE OF BANK'S COMMITMENT TO MICRO AND SMALL ENTERPRISES

Our bank has already adopted the code of Bank's commitment to Micro and Small Enterprises issued by Banking Codes and Standard Boards of India. Our dealings with Micro and Small Enterprises will be inline with the code of Commitment.

XI. CONCLUDING REMARKS

The loan policy for MSE sector will operate within the overall loan policy of the Bank and subject to guidelines/instructions of Regulatory Authorities/RBI/Government of India. Therefore, the policy will be amended with the approval of the Board whenever revised guidelines are received from the Regulatory Authorities.

This policy will be in force until a review is made by the Board of Directors for accommodating the emerging requirements.

GLOSSARY

1	BCSBI	Banking Codes and Standards Board of India
2	CRISIL	Credit Rating and Information Services India Ltd.,
3	CMA	Credit Monitoring Arrangement
4	CC	Cash Credit
5	CGTMSE	Credit Guarantee Trust for Micro and Small Enterprises
6	LG	Letter of Guarantee
7	LC	Letter of Credit
8	MSE	Micro and Small Enterprises
9	MPBF	Maximum Permissible Bank Finance
10	MSME	Micro, Small and Medium Enterprises
11	MSMED Act 2006	Micro, Small and Medium Enterprises Development Act 2006
12	MOU	Memorandum of Understanding
13	NABARD	National Bank for Agriculture and Rural Development
14	RAM	Risk Assessment Model
15	RBI	Reserve Bank of India
16	SIDBI	Small Industries Development Bank of India
17	SMERA	Small and Medium Enterprises Rating Agency

ANNEXURE

LOAN POLICY FOR MICRO AND SMALL ENTERPRISES SECTOR

EXISTING NORMS

Internal Scoring Model to be used for credit limits upto Rs.2 crores and Risk Assessment Model for limits of Rs.2 crores and above.
Current ratio of 1.25 is acceptable while lending under Naik Committee Norms.
Minimum 15% margin for loans above Rs.50000/- and upto Rs.5 lacs
Branch Managers upto the level of scale IV can sanction secured credit facilities to MSE units by taking collateral securities to a minimum extent of 60% of the limits sanctioned.
Setting up of MSE Loan Processing Centres at key locations
In exceptional cases, margins lesser than indicated in the policy can be prescribed with the approval of the appropriate authority as per powers delegated in bank's concession policy.
All Branch Managers can sanction collateral free loans to MSE sector with CGTMSE cover, upto their per borrower limits.
If term loan is sanctioned, working capital limit should also be sanctioned, if the same is not tied up with any other institution.
The interest payable up to six months after commercial production will be included as part of the project cost for assessment of credit requirements. Sufficient moratorium period say, upto six months, after commencement of commercial production, will be allowed for repayment of principal amount wherever required, to enable the unit establish itself in the market.
When the sanctioning authority decides to reject a MSE credit application, the same will be conveyed to the applicant only after obtaining approval from the next higher authority.