



Technical Assistance Consultant's Report

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January 2017

Sri Lanka: Small and Medium-Sized Enterprises Line of Credit Project (Financed by the Japan Fund for Poverty Reduction)

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Asian Development Bank



Performance Report January 2017

TA 9080 – SRI: Small and Medium-Sized
Enterprises Line of Credit Project

Preface

The SME Line of Credit is an initiative by the Ministry of Finance and the Asian Development Bank (ADB) where ADB will provide USD 100 million with the aim of channeling more funds to Sri Lankan firms that struggle to access the finance they need to grow. The ADB funds will be lent to participating financial institutions (PFIs) that will then lend the funds to small and medium-sized enterprises (SMEs). To access the funds, the PFIs have to bid successfully for the funds at eight semiannual auctions across four years.

This auction mechanism was introduced to create a market price for bank borrowings that are targeted for on-lending to the least-well served SMEs, such as new or rural borrowers or those led by women. As PFIs are likely to bid below their estimated marginal borrowing costs, they will maintain a financial incentive to disburse the funds. It is expected that the auction mechanism will address previous credit lines' difficulties in incentivizing PFIs to disburse the funds quickly and efficiently to SMEs.

Performance Analysis

The first auction was concluded on the 27th of April 2016 where 9 PFIs participated and one PFI, National Development Bank PLC (NDB), won the whole tranche of USD 12.5m at an interest rate of 6.01% (Annexure 1).

Performance is tracked against two broad parameters. First, the PFIs need to disburse the funds; the project will have no development impact if the funds remain undisbursed. Second, the funds once disbursed need to reach the intended borrowers.

Performance Analysis – Disbursement

On an absolute basis, disbursements have been strong, and almost the entire tranche was on-lent to SMEs in approximately a month's time (Table 1).

Table 1: Disbursement Summary

Fund Disbursement	
Disbursement Start Date	28 th July 2016
End of Reporting Period	11 th November 2016
Total Days	106 Days
Fund Utilization	
Total Auctioned Funds	LKR 1,821,832,500 (USD 12,500,000 equivalent)
Funds On-Lent to SMEs	LKR 1,821,832,500 (at exchange rate of 145.7466)
Utilization	100%

Disbursements are also strong on a relative basis. Compared to ADB's Small and Medium Enterprise Regional Development Project, which ran from 2008-2012, the auction mechanism's financial incentives are driving disbursements at a much faster rate (Table 2).

Table 2: Comparison with Previous SME Credit Lines

	Small and Medium Enterprise Regional Development Project (2008-2012)	SME Line of Credit (2016-2019)
Loans disbursed	\$40,371,325	\$12,500,000
Months	45.27 Months	3.14 Months
Rate	\$0.89 million per month	\$3.98 million per month ^a
^a Given funds are disbursed only semiannually, this rate is expected to decline to an average of approximately \$2 million per month over the project's lifespan.		

Performance Analysis – Development Indicators

In designing the credit line, the Ministry of Finance and ADB selected development indicators against which the project would be measured. These indicators focused on borrowers that are often excluded from the banking sector such as first-time borrowers or women-led SMEs.

Presently, the project is exceeding the development indicators. In particular, loans to first-time borrowers and women-led enterprises are well above their targets (Table 3). The one indicator that has performed poorly is working capital loans against which fixed or financial assets have not been pledged. This indicator aims to encourage cash flow lending. The underperformance could reflect the winner of the first auction's specific credit policies or the banking sector's general discomfort with cash flow lending. In any case, PFIs in subsequent auctions will only be allowed to extend working capital lines if fixed and financial assets are not pledged.

Table 3: Development Indicators

Criteria	Target	Actual	Success
The number of sub loans to SMEs borrowing from a commercial or specialized bank for the first time	≥ 10%	21.87%	●
The number of sub loans is to SMEs that are led by women	≥ 5%	23.75%	●
The amount of sub loans is lent cumulatively to "targeted SMEs"	≥ 50%	86.14%	●
SMEs where funds are used for subprojects outside of Colombo District	-	76.25%	
SMEs borrowing for working capital against which fixed or financial assets are not pledged	-	0.00%	
SMEs led by women	-	23.75%	
SMEs which had not previously borrowed from a licensed commercial or specialized bank.	-	21.88%	

Performance of Sub-loans

An analysis was carried out to evaluate the performance of the sub-loans as at 31st December 2016. The outcomes of the analysis are as follows:

Auction No.	Total Portfolio Value LKR	Total No. of Loans	Past Due			Non-Performing Loans			Write Downs		
			No. of Loans	Amount LKR	Avg No. of Days Outstanding	No. of Loans	Amount LKR	Percent age (%)	No. of Loans	Value LKR	Percent age (%)
1	1,522,345,354	160	42	402,480,287	26	0	0.00	0.00%	0	0	0.00%

Additional information on the SMEs assisted under the program is included in Annexure 2.

Annexure 1: Summary of First Auction Bidding

Bank Name	Bid Rate	Bid Amount	Allocated Amount
National Development Bank	6.01	12,500,000	12,500,000
Sampath Bank	5.03	12,500,000	0
Commercial Bank of Ceylon	5.01	5,000,000	0
Nation's Trust Bank	4.90	5,000,000	0
DFCC	4.50	4,000,000	0
Peoples Bank	4.01	3,000,000	0
Hatton National Bank	4.00	8,000,000	0
Seylan Bank	3.80	3,000,000	0
Bank of Ceylon	2.51	3,000,000	0

Annexure 2: Summary of SME Lending

Fund Disbursement	
Bank	NDB Bank PLC
Total Value of Loans Disbursed (LKR)	1,821,832,500 .00
Utilization of SME Credit Line (LKR)	1,821,832,500.00
Funds Unutilized (LKR)	-
Summary of SME Loans	
Total Number of Loans Disbursed	160
Average Upfront fee (LKR)	256,763
Average Interest Rate	11%
Average Interest Rate vs. Average Weighted Prime Lending Rate (AWPLR)	0.21% points below 6-month AWPLR as of 30 th September 2016
Average Margin over Funding Cost	5%
Average Tenor (Months)	59
Average Equity Contribution of SMEs to Total Subproject Amount	32%
SMEs' Average Annual Turnover	220,585,009
SMEs' Average Number of Employees	30
Rate Analysis	
Interest Rate	Percentage of Total Loans
9% - 10%	4%
10% - 11%	88%
11% -12%	5%
12% - 13%	4%
13% - 14%	1%
Margin Over Funding Cost	Percentage of Total Loans
3% - 4%	3%
4% - 5%	85%
5% - 6%	8%
6% - 7%	3%
7% - 8%	1%

Previous Loan Taken from PFI
(Percent of Disbursements)

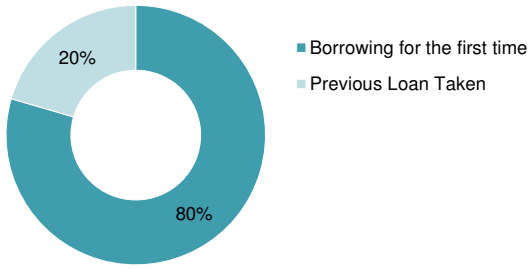


Chart 01

Collateral Type
(Percent of Loans on Type of Collateral)

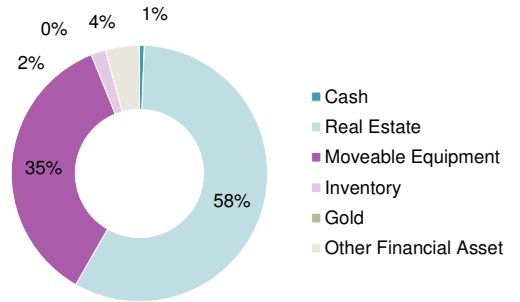
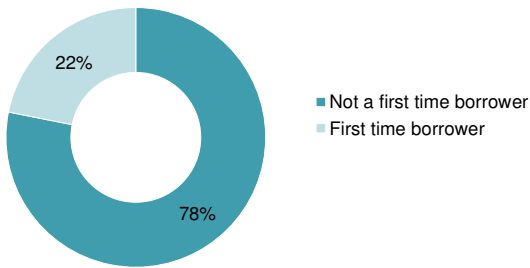


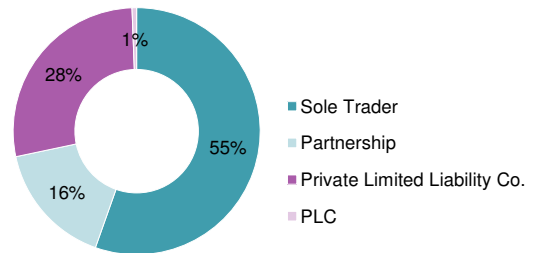
Chart 03

Out of 160 loans disbursed, only one was given without obtaining collateral, i.e. 99% of the loans were collateralized.

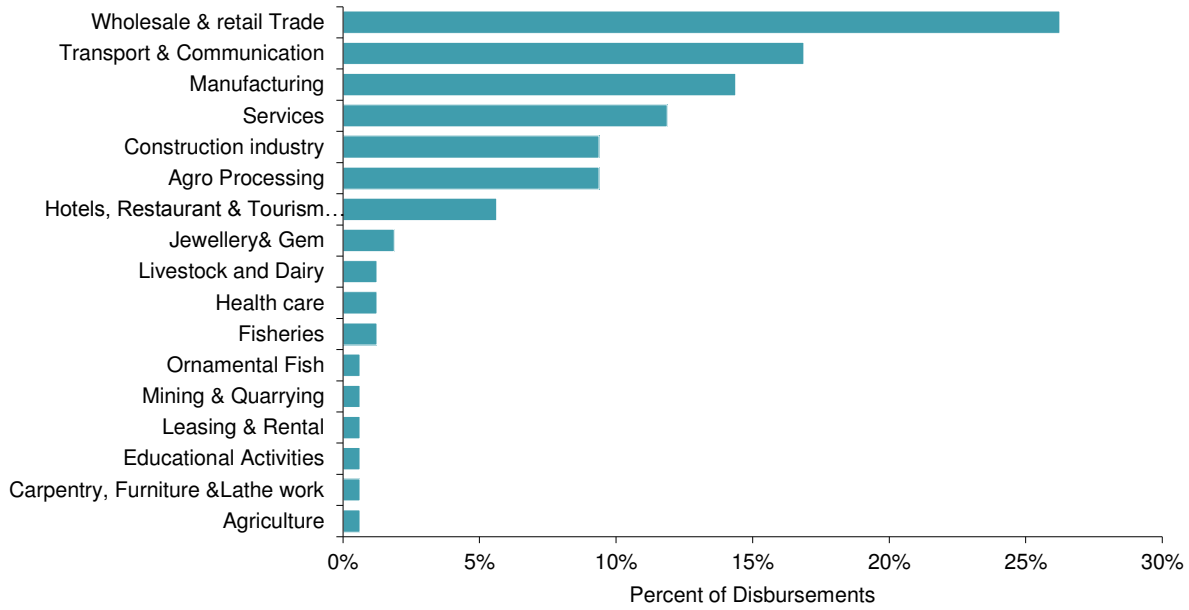
First Time Borrowers
(Percent of Disbursement)



Legal Structure
(Percent of Disbursements)



Sector Activity



District of Borrower's Project

