



SAARC

SAARC Development Fund

**Policy Guidelines
For
Economic
And
Infrastructure
Windows
of SDF**

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1. Introduction

SAARC Development Fund (SDF) was established in April 2010 to serve as the umbrella financial institution for SAARC projects and programs which are in fulfillment of the objectives of the SAARC Charter. As per Article 4 of SDF Charter defined in Volume I : Legal Documents, SDF has three funding windows viz. Social Window , Economic Window and Infrastructure Window. These policy guidelines have been framed for Economic and Infrastructure Windows. Under the Economic and Infrastructure (E&I) Windows (E&I Windows are defined in the Article 4 of SDF Charter), SDF will finance projects as per the identified areas of focus –these are elaborated under Para 3 of this document.

2. Purpose:

The purpose of this Guideline is to set forth terms and conditions applicable to loans to be made by SDF under its E&I Windows. This E&I Policy Guidelines document will act as one of the operational document for project financing by SDF.

3. Priority Areas for Economic and Infrastructure Windows

Under Economic and Infrastructure Windows, SDF will focus on financing projects pertaining to the following sectors:

Economic Window:

- a) Trade and Industrial Development
- b) Agriculture and allied sectors
- c) Services Sector
- d) Science and Technology
- e) Other Non-Infrastructure areas
- f) Any other sectors as approved by the Board

Infrastructure Window:

- a) Energy,
- b) Power
- c) Transportation
- d) Tele Communications
- e) Environment
- f) Tourism
- g) Other Infrastructure Areas.
- h) Any other sectors as approved by the Board

4. Eligible Projects:

Eligible Borrowers:

The loans under the two windows could be extended to general government and public sector corporate bodies entities, SPVs , private sector . Thus, no assistance is envisaged to sole proprietorships, partnership firms (even Limited Liability Partnerships), trusts and NGOs in the initial phase

As per Article 5 of the SDF Charter, the resources and facilities may be utilized for funding:

- a) Projects/programs involving any one or more than one SAARC Member State with the direct benefit going to more than one Member State.
- b) Projects located in one SAARC Member States of significant economic interest for two or more SAARC Member States; and
- c) Projects with significant focus on poverty alleviation as envisaged under the Economic & Infrastructure Windows in any SAARC Member State having thematic linkage with more than two SAARC Member States as part of sub – regional project

4.1 Priority Areas: The SDF shall assign priority to those projects which:

- a) Have high potential for positive regional economic impact by benefiting at least two SAARC Member States.
- b) Promote cooperation among Member States.
- c) Have strong potential for facilitating mobilization of domestic and foreign capital.
- d) Are commercially viable, and operationally sustainable;
- e) Source and utilize raw materials, equipment and other productive inputs within the SAARC region.
- f) Create and promote intra -SAARC trade.
- g) Promote backward, forward and spatial linkages in economies of SAARC Member States.
- h) Develop and promote indigenous and appropriate technologies and skills.
- i) Promote majority ownership and management by SAARC nationals.
- j) Promote the role of women in trade and overall development.
- k) Comply with international acceptable environmental protection standards.
- l) Create and expand employment opportunities and other social benefits.
- m) Are export-oriented, local resources based and regional in nature.

5. Products to be offered

- a) As per Article 5(3) of the Charter, the Fund shall primarily finance long term priority regional programs and projects.
- b) As per Section 7 of Bye-laws, the Fund shall carry out its operations in furtherance of its purpose and functions as set out in the Charter in the following ways:
 - i. by making or participating in direct loans;
 - ii. by guaranteeing in whole or in part, loans for economic development and serving other objectives of the Fund, participated in by the Fund.

- iii. by facilitating access to domestic and international capital markets by institutions or enterprise through the provision of guarantees, where other means of financing are not appropriate, and through financial advice and other forms of assistance.
- iv. by deploying other resources, in accordance with the agreements determining their use,
- v. by managing its idle funds in a prudent and beneficial manner; by or through such other financial instruments, as the Governing Council may decide.
- vi. Funds available in the shape of main corpus will not be utilized for funding and activation of E&I windows. In the initial period, E&I Windows will be funded out of the interest income earned/to be earned by SDF on its main corpus plus the funds to be raised by SDF.

6. Defining Direct Benefit: Direct benefit going to more than one Member State may be defined to include cross border Trade & Commerce, Infrastructure, Projects resulting in significant value of exports on continuous basis between more than one Member State like in the case of Manufacture and supply of intermediary products to other Member State, Equity investment from one Member State into another by public or private sector companies (FDI) or any other criteria as decided by the Board, considering the unique needs of any project/s.

7. Asset Allocation: In the long term, the Fund will have to deploy meaningful investment amount per project to have any impact and also maintain adequate influence on the project/programme. At the same time, effective diversification for risk mitigation and achievement of its investment objectives will have to be balanced. The purpose of diversification is to ensure that no single investment/ project, country exposure or national or regional or political or economic events will disproportionately affect the SDF's viability and its returns.

Given these objectives, the following exposure control (as per the 26th Board Meeting of SDF) is proposed for the SDF's Economic & Infrastructure windows investments:

- a) **Project Ceiling:** SDF will consider the projects where SDF credit exposure will be maximum up to US\$ 15.00 million (contribution by the promoter as the owner's equity would be 25% of the SDF maximum credit exposure) or 75% of the Engineering Procurement Construction (EPC) Cost, whichever is lower. The maximum loan period will be 10 Years including 2 years of grace period ;
- b) SDF should follow the principle of equity among the Member States for allocation of the funds for different projects.

Exposure Caps

As per Section 8 of SDF Bye-Laws, the total amount of outstanding loans and guarantees made by the Fund shall not any time exceed the total amount of its unimpaired subscribed capital, reserves and surplus included in the monies of the Fund.

As per Section 10(2)(iv) of the SDF Bye-Laws, the Fund shall seek to maintain reasonable diversification in all its lending operations . SDF will cap its exposure to various sectors and Member States, as a prudent Credit Risk Management measures.

8. Funding Mechanism/Disbursement Procedure

Disbursement: The term “disbursement” refers to the withdrawal of proceeds from the SDF financed grant or loan account.

The procedure for withdrawing the loan proceeds for the purpose of carrying out a project will be governed as per the *SDF Credit Manual - Book 3 : Disbursement Procedures, which is reproduced below:*

The disbursement methods selected during project approval are based on project characteristics, the categories of expenditures to be financed and the capacity of the executing agency to manage project resources. Disbursements are made using one or, a combination of the methods outlined below:

a. Reimbursement

The SDF may reimburse the borrower for the expenditures eligible for financing that are in compliance with the loan agreement.

b. Reimbursement Guarantee

In this disbursement method, the SDF provides an irrevocable undertaking to reimburse a commercial bank for payments made or to be made to a supplier against a letter of credit.

c. Special (Designated) Account

In this disbursement method, the SDF will make an advance disbursement from the loan account to special account. However, before the SDF authorizes establishments of a special account, the borrower must have adequate administrative capability, internal controls, and accounting and auditing procedures to ensure effective use of these special accounts.

d. Direct Payment

In this disbursement method, at the borrower’s request, the SDF may agree to pay designated agency/suppliers directly for eligible expenditures.

Reinvestment of any undisbursed fund (principle and interest) – Any undisbursed/unutilized fund (principle + interest) has to be returned to the SDF by the borrower .

9. Terms and Conditions for Project Financing

a. Project financing through Direct Loans:

This shall be various financing/ credit facilities offered by SDF. Need based medium term / long term loans will be extended to borrowers to meet diverse needs of the clients. The products will have to be tailored to meet specific requirements of the clients.

b. Security and documentation:

All the loans shall be secured. Security creation and legal documentation shall be made as agreed with the

consortium/syndication, on a case to case basis, also considering the unique legal requirements in each SAARC Member State.

However under Co-Financing, the project or any terms and conditions related to the project financing shall not violate any of the terms and conditions as laid down by the SDF Charter and Bye Laws.

c. Preparation of security documents

After obtaining clearance on title from CEO, the following documents should be prepared by SDF Legal department, viz.

- a) Board Resolution to be passed by the Company;
- b) Declaration and Undertaking (in case of equitable mortgage);
- c) Memorandum of Entry (in case of equitable mortgage);
- d) Indenture of Mortgage (in case of mortgage other than equitable mortgage).
- e) Any other document as per the Board directions or required under the Project Proposal on case-to-case basis.

9.1 Financing Process: Financing process for the projects under the two windows of SDF is as below:

a) Business or Economic Assessment

To analyze the business operations and thus economic development impact on the respective SAARC Member States.

b) Technical Assessment

To analyze the management capacity to carry out the project, implementing the latest technologies. Also to understand the technology development to be occurred through the project in the respective SAARC Member States.

c) Financial Assessment

To analyze the financial/ credit strength and loan repayment capacity of the borrower. It includes the analysis of Financial Statements, Ratio Analysis, Bank Statements etc.

d) Environmental and Social Assessment

To understand that whether the project is compiling all the necessary Environmental Laws etc in the respective SAARC Member States.

e) Legal Assessment

To understand the legal framework of the respective SAARC Member States.

f) Risk Assessment

To understand the various risks associated with the project proposal, that includes Country Risk, Economic Risk, Legal Risk, Currency Risk, Exposure Risk, Business Risk, Political Risk, Interest Rate Risk, Market Risk, Operation Risk, Default Risk, Liquidity Risk, Sustainability Risk etc.

The funding mechanism under the Economic & Infrastructure windows will be 100% Loan.

9.2 Financing Terms and Conditions.

Certain terms and considerations that must be followed by SDF while financing a project-

- (a) The amount of any equity investment shall not exceed such percentage of the equity capital of the entity or enterprise concerned as permitted under policies approved by the Board of Directors.
- (b) Following disbursement procedure will be applied as per the approved Disbursement Procedures of SDF:
 - i. Reimbursement
 - ii. Reimbursement Guarantee
 - iii. Special (Designated) Account and
 - iv. Direct payment
 - v. Depending on project requirements a combination of aforesaid methods may be used for disbursement with the approval of the Board.
- (c) Disbursements will be made as per agreement.
- (d) Borrowers shall be required to open such Special (Designated) accounts for SDF funding exclusively.
- (e) For term loans sanctioned to projects under joint finance / consortium arrangement, the terms and conditions, including interest rate, stipulated by the lead institution /other banks will normally be followed. Terms and conditions under joint financing arrangements will be determined based on what the market will bear for specific types of risk/tenor at the time a facility is being syndicated. However under Co-Financing, the project or any terms and conditions related to the project financing shall not violate any of the terms and conditions as laid down by the SDF Charter and Bye Laws.
- (f) The undertakings relating to-
 - i. Environmental and social aspects of the Project,
 - ii. Procurement of goods and services required for the Project (if applicable) and
 - iii. Integrity will be governed by SDF Charter & Bye Laws.
- (g) Signing of the Legal Agreements will takes place: (a) after the Financing has been approved; and (b) all required signing authorizations are received.
- (h) For each proposed Project, the Fund requires that the Project meet the following conditions:
 - i. The Project has clearly defined development objectives consistent with SDF Charter and bye laws and permit appropriate evaluation of the Project's impact.
 - ii. The Project should have specific productive activities necessary to meet development objectives of SDF.
 - iii. Alternative sources of finance, in particular private capital, are unavailable for the Project on terms and conditions that the Fund considers reasonable.

- iv. The Project is in compliance with the requirements of this Policy and other applicable policies.
- (i) Benchmark Financial Norms will be applicable as per the respective point mentioned in this Economic & Infrastructure Policy guidelines.
- (j) Computation of Interest Charged: The interest charge shall be computed on the basis of 360-days a year having Twelve Months of 30 days each. Repayment and Prepayment:
 - i. The Borrower shall pay the principal amount of the Loan withdrawn from the Loan Account in accordance with the amortization schedule to the Loan Agreement.
 - ii. After giving not less than 30 days' written notice to SDF, the Borrower shall have the right to repay in advance of maturity, as of a date acceptable to SDF (provided, that the Borrower shall have paid all amounts due under the Loan Agreement as of such date).
- (m) For any matter related to financing the various projects, provisions of legal agreement will be applicable.
- (n) No Connected Lending will be permitted.

10. Co-financing:

SDF will participate in co-financing to minimize risk and to gain institutional experience of funding in the region. Co-funding agencies shall be commercial banks, regional financial institutions, or the other similar type of organization.

As per Section 10(1)(vi) of the SDF charter, the Economic & Infrastructure Windows should as far as possible, finance projects in collaboration with MDBs, national, regional and international agencies, to maximize development impact.

SDF will rely on due diligence of the lead banker/local/ regional financial institutions and their market reports. SDF will also rely on their project appraisals. However under Co-Financing, the project or any terms and conditions related to the project financing should not violate any of the terms and conditions as laid down under the SDF Charter and Bye Laws.

11. Benchmark Financial Norms

For term loans, the following benchmark financial norms are proposed:

Sl. No	Financial Parameter	Norm
1	Debt Equity Ratio (DER) (For the company as a whole, including proposed assistance)	3:1 (Maximum)
2	Promoter's / Owner's contribution for the project (Definition of promoter would be reviewed on a project to project basis)	25% (Minimum)
3	Liquidity Support - Debt Service Coverage Ratio (DSCR) Revenue generation by the Project will also be taken into consideration at the time of evaluating the Debt Repayment capacity of the borrower.	1.5:1

4	Sustainability - Asset Coverage As per Credit Manual Book-1 : Appraisal, Overall Asset Coverage = Total Tangible Security including collateral security / term loan	1.3:1 (Minimum)
5	Repayment Period	Maximum 10 years
6	Maximum Grace period for repayment	2 years
7	Maximum amount of Exposure	USD 15 Mn (after USD 3.75 Mn contribution from the promoter) or 75 % of the EPC amount (whichever is less)

a) For Promoter's/ Owner's Contribution, please refer Credit Manual Book-1 : Point # F on Page # 36.

b) For DSCR please refer Credit Manual Book-4 : Follow-up & Monitoring point # 20 on page # 17.

c) For policies regarding lending under Consortium, please refer Credit Manual Book-1page # 57.

12. Provision of Currency:

1. As per Section 9 of the SDF, in making direct loans or participating in them, the Fund may provide financing in any of the following ways:

- a) By furnishing the borrower with currencies other than the local currency, which are necessary to meet the foreign exchange costs of a project ; or
- b) By providing funds to meet local expenditures on the project concerned, where it can do so by supplying local currency without selling any of its holdings in convertible currencies.

In the initial period the Fund shall finance in international currencies, mainly in USD as well as in local currencies of Member States. The local currency loan rates would be considered on a project to project basis based upon the market rates, opportunity cost etc.

13.Pricing for Project financing:

Pricing of the loan under the Economic & Infrastructure Windows shall be 6 months LIBOR plus 2% fixed spread plus applicable fees as mentioned in the E&I Policy guidelines .This pricing is applicable for all SAARC Member States or the SAARC Member States participating in the Project Proposal.

Charges	Amount	Process
Appraisal Fee (Fees towards Project appraisal including Credit Appraisal, Risk Analysis Legal study etc.)	Maximum 0.25% of the term loan sanctioned by SDF.	To be collected before taking up detailed appraisal of the project.
Up-front Fee (To be collected at the time of 1 st Disbursement)	1.0% of the term loan sanctioned by SDF. If co-lenders are there it will as per co-funding terms of sanction.	To be collected after sanction and before issue of term sheet.
Documentation Fee (For executing the various loan documents including cost incurred on paying the Stamp Duty while executing the various loan documents)	To be charged on cases to case basis up to maximum of 0.25% of term loan sanctioned.	
Commitment Fee (For ensuring the disbursement of the sanctioned limits)	0.50% p.a. (on the undisbursed amounts of loan accruing from the date of the Loan Agreement until the time of disbursements of such amount).	To be collected based on disbursement pattern.
Prepayment Charges (in case if the borrower prepay the part-loan of the entire loan before the maturity date)	Prepayment charges to be taken from the borrower on a case-to-case basis.	Request from the borrower to SDF for prepayment of loan.
Late payment charges (To be taken if the borrower fails to repay the EMIs or the loan component on time as Stipulated in the sanction letter)	2% penalty on all late payments including principal and interest i.e on Loan outstanding (As per the Credit Policy approved in the 19 th Board Meeting held on 6-8 August in Islamabad, Pakistan).	To be collected at the earliest or along with next repayment.

14. Fair Practices Code:

SDF shall adopt transparent approach with respect to eligible projects, appraisal, sanction/disbursement, monitoring and supervision, interest rates, pre-payment clauses, grievance-redressal, costs to be borne by borrowers, and such other policy and operational matters.

15. Project Roadmap and Approval Process.

Under the Economic & Infrastructure windows, the roadmap for the approval on the various projects covers the below stages with their respective time frames-

- a) identification of the eligible projects,
- b) conducting an internal robust credit appraisal within two weeks, which includes eligibility (as defined in the SDF Charter and Bye Laws) check, KYC checking, to check the project compliance towards Social & Environmental safeguard compliance, Due Diligence or any other aspect as directed by the Board of Directors/ CEO or required under the project proposal on case to case basis.
- c) Referring the project proposal to the appraisal committee formed by the SDF Board to undertake the detailed project appraisal.
- d) Approval from the SDF board on the project proposals as referred by the appraisal committee formed by the SDF Board.
- e) signing of the Project Finance Agreement (PFA) after approval from the Board within four weeks,
- f) after signing of PFA, execution of the various security documents, within two weeks and
- g) after completion of signing of all legal documents , disbursement of the loan within 1 week, as per the sanctioned terms and conditions.

Proper Risk Management practices to be adopted for the close monitoring and proper utilization of the SDF funds by the borrowers. A sound legal framework to be established to ensure the dispute resolution (if any).

16. Proposals need approvals from the SDF Board: All project proposals to be sent to the Project Approval committee set up by the SDF Board for their review and necessary approvals.

17. Follow-up and monitoring

Regular and proper follow-up and monitoring of borrower accounts are key to building a quality portfolio which cannot be done by mere sanction of assistance. Activities related to disbursement, proper utilization of funds, achievement of physical results projected at the time of appraisal, periodic review of implementation / operation and prompt servicing of assistance are important aspects. The lender has to build a long term relationship with the borrower in mutual interest. Follow up commences soon after sanction aimed at achieving the goal and optimizing the benefits of investment within the opportunities available and constraints present. Key objectives of follow-up and monitoring (as defined in the Credit Manual Book 4) are –

- a) Proper utilization of assistance /end-use of funds;
- b) To ensure implementation within cost and time originally estimated.
- c) Compliance with terms and conditions of sanction;
- d) That securities offered / charged / documentation are in order;
- e) Detection of warning signals, such as deterioration in credit quality / financial;
- f) Performance of the account, changes in management structure, reconstitution;

- g) Death or resignation of a key person, and other causes of concern leading to possible failure of the firm;
- h) To anticipate problems and reorient policies / procedures.
- i) To carry out evaluation of operations of the unit;
- j) To utilize the feedback for project appraisal and policy formulation;
- k) To ensure viable operations of the unit.

This is a crucial aspect of lending to ensure end-use of funds. The Fund shall take the necessary measures to ensure that the proceeds of any loan made, guaranteed or participated in by the Fund, are used only for the purposes for which the loan was granted.

The SDF may engage reputed financial experts, preferably Chartered Accountant firms in Member States, to furnish progress reports on the projects financed by SDF, wherever required.

18. Material Changes to the Project or Financing:

Following approval of the Financing, as well as during implementation of the Project, the Fund will normally not agree to make any material change in the Project or its financing agreement. However, in exceptional circumstances, the request of borrower may be considered by the SDF Board to respond to changed circumstances of the various SAARC Member States but any material change should not change the scope and focus of the project.

19. APPLICABLE GOVERNING LAW

Funding under the Economic & Infrastructure Windows is governed by and shall be construed in accordance with the laws of the Member State within whose territorial jurisdiction the Project under this Agreement is implemented.

20. DISPUTE RESOLUTION.

In the event of any disputes that arise between the lender (SDF) and the borrower, the parties to the loan / guarantee will attempt in good faith to resolve such dispute. In case the dispute cannot be otherwise resolved, the parties shall consider settling dispute through SAARC Arbitration Council and the decision of such arbitration shall be final and binding to all concerned parties

21. FUNDS RECOVERY.

In the event of any default, possible ways for the recovery of funds are as below:

- a) Settling outstanding overdue loan by selling-off the collateral at the prevailing market rates in the respective SAARC Member States.
- b) Initiate the debit freeze and debit the borrower's Escrow Account/Special Designated Account, opened for remitting the project cashflows.
- c) In case if the equity shares of the borrower are pledged with SDF, then in the event of default by the borrower, the borrower's shares (pledged with SDF) will be sold by SDF in the open market, to recover the outstanding loan/ overdue loan.
- d) Exercise any other method as directed by the Board of Directors undertaken as the legal course of action.
- e) Unutilized Fund: to be returned to SDF along with interest earned.