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Research & Insights

Risk Assessment of the SME Financing Portfolio and Forecast of Guarantee Scheme Liabilities

Q3 2023 – Q2 2025

Executive Summary

This report presents a comprehensive risk assessment of the Small and Medium Enterprise (SME) financing portfolio in Pakistan for the eight-quarter period from Q3 2023 to Q2 2025. The primary objective is to analyze the portfolio's evolution, identify key risk concentrations, and provide a robust forecast of the fiscal liabilities arising from the State Bank of Pakistan's (SBP) Risk Coverage Scheme (RCS) to inform budgetary planning for the Ministry of Finance.

The analysis reveals a period of unprecedented and policy-driven expansion in SME credit. Total outstanding financing grew by PKR 250.[1] billion between August 2023 and June 2025, reaching a total portfolio size of PKR 761.6 billion.[1] This growth was significantly catalyzed by the introduction of the RCS on July 1, 2024, which prompted a 173.3% acceleration in average monthly net credit additions from PKR 6.3 billion pre-RCS to PKR 17.2 billion post-RCS.[1]

This expansion, however, has introduced significant concentration and credit quality risks. The portfolio is heavily skewed towards two sectors: Wholesale & Retail Trade and Manufacturing, which collectively account for 68.4% of total exposure as of June 2025, making the portfolio highly susceptible to macroeconomic shocks affecting consumer demand and industrial activity.

A critical emerging risk stems from a fundamental shift in lending dynamics during the first half of 2025. The period saw an influx of over 92,600 new borrowers, concurrent with a sharp decline in the average loan size to PKR 2.50 million.[1] This trend accelerated dramatically in the most recent quarter (Q2 2025), with the average ticket size for new loans dropping to just PKR 1.40 million.

Critically, this latest surge has been dominated by "clean loans" extended with no collateral, significantly elevating the potential Loss Given Default (LGD) for this vintage. This indicates a pivot to high-volume, unsecured, and transactional lending to smaller, potentially less resilient enterprises.

Quantitatively, after recalibrating risk parameters to account for the unsecured nature of recent lending, the base-case Expected Loss (EL) for the entire SME portfolio is calculated at PKR 41,722 million. This assumes a forward-looking Probability of Default (PD) of 9.5% and a blended LGD of 57.7%, which incorporates the higher LGD on the new unsecured loans.[3] For the portion of the portfolio covered by the RCS, the Ministry's direct first-loss exposure is estimated at PKR 27.1 billion. The central forecast for the 12-month fiscal liability against this exposure is estimated at PKR 2.30 billion. However, a prudent stress scenario, which accounts for the elevated risk profile of the newly acquired unsecured borrowers, indicates a potential liability of PKR 3.66 billion.

This report recommends that the Ministry of Finance adopt a tiered budgeting approach for RCS claims, engage with the SBP for more granular performance data on the post-RCS loan vintage—with a specific focus on collateral levels—and implement targeted monitoring of high-risk sectors to proactively manage the evolving fiscal risk.

(Q3 2023 – Q2 2025)

1. Macro-Level Trends in SME Financing

The past two years have marked a transformative period for SME financing in Pakistan. The landscape has been reshaped by aggressive credit expansion, a pivotal policy intervention, and a consequential shift in the fundamental structure of the loan portfolio. This section examines these macro-level trends to establish the context for the detailed risk assessment that follows.

1.1. Overall Portfolio Evolution

The total outstanding financing to SMEs has demonstrated significant growth, albeit with notable volatility between quarters. The portfolio expanded from PKR 517.7 billion at the end of September 2023 to PKR 761.6 billion by the end of June 2025, representing a total increase of 47.1% over the eight-quarter period.[1]

Analysis of the quarterly growth patterns reveals distinct phases. A strong expansionary phase was observed in Q4 of both 2023 and 2024, with quarter-on-quarter (QoQ) growth reaching 17.02% and 16.97%, respectively. These surges are often followed by periods of consolidation or contraction, such as the -7.64% QoQ decline in Q1 2024. However, the 15.65% QoQ growth registered in Q2 2025 represents a significant break from this pattern, signaling a new, aggressive growth dynamic in the most recent period under review.[1] Year-on-year (YoY) growth figures underscore the accelerating momentum, rising from 10.62% in September 2024 to a substantial 32.55% by June 2025.

Quarter End	SME Outstanding (PKR mn)	QoQ Growth (%)	YoY Growth (%)
Sep-2023	517,676.9	-	-
Dec-2023	605,774.0	617.02%	-
Mar-2024	559,486.1	-7.64%	-
Jun-2024	574,572.3	2.70%	-
Sep-2024	572,657.5	-0.33%	10.62%
Dec-2024	669,830.7	16.97%	10.57%
Mar-2025	658,491.7	-1.69%	17.70%
Jun-2025	761,576.8	15.65%	32.55%

Data Source: NCGCL Memo, SBP Data Files

This chronological overview provides the foundational context for the entire report, establishing both the scale and the accelerating velocity of change within the national SME portfolio.

1.2. The Impact of the SBP Risk Coverage Scheme (RCS)

The most significant catalyst for the observed growth acceleration was the implementation of the SBP's Risk Coverage Scheme (RCS) for SMEs, effective July 1, 2024.[2] The scheme was designed to mitigate credit risk for participating financial institutions by providing first-loss coverage on the principal portion of fresh or incremental SME financing. The government agreed to absorb 20% of the first loss for Small Enterprises (SEs) and 10% for Medium Enterprises (MEs) for loans with a tenor of up to five years.

The market's response to this policy intervention was immediate and profound. A "before and after" analysis centered on the July 1, 2024, start date reveals a structural break in lending trends. In the 11-month period prior to the scheme's launch (August 2023 – June 2024), average monthly net additions to the SME portfolio stood at PKR 6,307.5 million. In the 12 months following its implementation (July 2024 – June 2025), this figure surged by 173.3% to an average of PKR 17,238.3 million per month.

Period	Duration (Months)	Total Net Additions (PKR bn)	Average Monthly Net Additions (PKR bn)	Compound Monthly Growth Rate (%)
Pre-RCS (Aug 2023 – Jun 2024)	11	69.4	6.3	1.19%
Post-RCS (Jul 2024 – Jun 2025)	12	206.9	17.2	2.67%

This sharp inflection provides unequivocal evidence of the RCS's powerful effect on credit supply. It suggests that the primary constraint on SME lending was not a lack of bank liquidity but rather the perceived high risk of the sector. By providing a government-backed backstop, the scheme effectively lowered the risk threshold for banks, encouraging them to extend credit to segments they previously deemed commercially unviable. The direct consequence is that the post-RCS loan vintage is composed of a riskier pool of borrowers who were previously screened out by conventional underwriting standards. The government, through the guarantee, has therefore assumed exposure to a higher-risk stratum of the SME market that the private sector was unwilling to finance independently.

1.3. Borrower and Ticket Size Dynamics

Concurrent with the surge in lending volume, the composition of the SME loan book has undergone a dramatic transformation. The data reveals a clear and accelerating trend away from larger, fewer loans towards a high-volume, low-value lending model. This shift is most pronounced in the first half of 2025.

Between December 2024 and June 2025, the total number of SME borrowers increased by 92,606, a remarkable 50.3% jump in just six months. During this same period, the average loan size (ticket size) across the portfolio fell sharply by 28.3%, from PKR 3.49 million to PKR 2.50 million.[1]

1.3

Quarter End	Borrowers (count)	Outstanding (PKR bn)	Average Ticket Size (PKR mn)
Sep-2023	165,080	438.05	2.654
Dec-2023	172,292	542.53	3.149
Mar-2024	174,880	488.83	2.795
Jun-2024	176,246	490.96	2.786
Sep-2024	177,753	478.37	2.691
Dec-2024	183,987	641.35	3.486
Mar-2025	203,139	584.44	2.877
Jun-2025	276,593	690.98	2.498

Data Source: NCGCL Memo, SBP Data Files

This dynamic is a primary indicator of the changing nature of the risk being underwritten. The rapid growth in borrower numbers alongside a shrinking ticket size signals a fundamental shift from traditional, relationship-based SME lending—which typically involves deep underwriting for a smaller number of larger clients—to a more transactional, programmatic approach. Such models rely on simplified credit scoring and automated processes to handle high volumes efficiently but carry higher inherent credit risk due to less rigorous individual assessment.

For the Ministry of Finance, this structural shift has critical implications for the nature of its contingent liability under the RCS. The risk is no longer confined to managing a few potentially large defaults but has evolved into managing a high-frequency stream of smaller, more numerous claims. This transformation necessitates different administrative, monitoring, and budgetary capabilities to handle a high-volume claims environment effectively.

2. Sectoral Deep Dive and Concentration Analysis

Dissecting the portfolio by economic sector reveals where the policy-induced growth has been concentrated and, consequently, where the government's financial exposure is most significant. The analysis shows a portfolio characterized by a lack of diversification, with risk heavily consolidated in sectors closely tied to the domestic economy's performance.

2.1. Portfolio Composition and Concentration

As of June 2025, the SME financing portfolio exhibits a profound concentration risk. Two sectors-G. Wholesale & retail trade; repair of motor vehicles and motorcycles, and C. Manufacturing-dominate the landscape, collectively accounting for 68.38% of the total outstanding amount of PKR 761.6 billion.[1]

Sector	Outstanding (PKR million)	Share (%)
G. Wholesale & retail trade; repair of motor vehicles and motorcycles	261,558.9	34.34%
C. Manufacturing	259,264.2	34.04%
A. Agriculture, forestry and fishing	67,377.9	8.85%
Q. Other service activities	51,600.9	6.78%
H. Transportation and storage	44,041.0	5.78%
F. Construction	20,447.6	2.68%
Others	55,283.1	7.23%
Total	**761,576.8**	**100.00%**

Data Source: NCGCL Memo, SBP Data Files

This heavy concentration makes the portfolio, and by extension the government's guarantee scheme, exceptionally vulnerable to macroeconomic shocks. The Wholesale & Retail Trade sector is directly exposed to fluctuations in consumer demand, inflation, and household disposable income. Similarly, the Manufacturing sector is highly sensitive to changes in input costs (such as energy and imported raw materials), supply chain integrity, and both domestic and international demand cycles. An adverse event affecting any of these variables, for instance, a sharp currency devaluation or a spike in energy prices, would not be a peripheral issue for the portfolio; it would directly impact its core 68%. The financial health of the RCS is therefore disproportionately tethered to the performance of these two key economic pillars.

2.2. Key Drivers of Two-Year Growth

An analysis of the portfolio's growth drivers from August 2023 to June 2025 confirms that the existing concentration has been reinforced by recent lending patterns. Of the PKR 250.1 billion in net new financing over this period, the Wholesale & Retail Trade sector was the single largest contributor, accounting for PKR 95.5 billion, or 38.20% of the total increase. Manufacturing followed, contributing PKR 56.2 billion (22.46%).[1]

Notably, other sectors also made significant contributions, indicating a broadening, if still concentrated, base of growth. The Agriculture, forestry and fishing sector added PKR 37.9 billion (15.16% of growth), while Transportation and storage and Other service activities also played important roles.[1]

Sector	Outstanding (Aug 2023 – Jun 2025) (PKR mn)	Contribution to Total Growth (%)
G. Wholesale & retail trade; repair of motor vehicles and motorcycles	95,531.2	38.20%
C. Manufacturing	56,164.4	22.46%
A. Agriculture, forestry and fishing	37,915.9	15.16%
H. Transportation and storage	23,414.8	9.36%
Q. Other service activities	22,924.0	9.17%
Total (all sectors)	**250,079.3**	**100.00%**

Data Source: NCGCL Memo, SBP Data Files

2.3. Analysis of Recent High-Growth Quarters

A more granular examination of the two most significant post-RCS growth quarters—Q4 2024 and Q2 2025—reveals a telling evolution in banks' risk appetite under the government guarantee.

In the immediate aftermath of the RCS launch, the lending surge in Q4 2024 was overwhelmingly directed towards the Manufacturing sector, which captured 52.28% of the quarter's total net increase. This suggests that banks initially channeled their expanded lending capacity towards a familiar, asset-heavy sector where credit risk assessment is more established.

However, by Q2 2025, the growth drivers had shifted markedly. The Wholesale & Retail Trade sector became the primary recipient of new credit, accounting for 45.89% of the quarterly growth. More strikingly, the "Other service activities" sector emerged as the second-largest contributor, absorbing 23.20% of the net increase—a dramatic rise from its 3.43% share in the Q4 2024 expansion.

Sector	Share of Quarter Growth (Q4 2024)	Share of Quarter Growth (Q2 2025)
C. Manufacturing	52.28%	8.53%
G. Wholesale & retail trade	29.49%	45.89%
Q. Other service activities	3.43%	23.20%
A. Agriculture, forestry and fishing	7.68%	9.18%
H. Transportation and storage	5.19%	4.55%

Data Source: NCGCL Memo, SBP Data Files

This pivot demonstrates a classic pattern of risk migration often observed in markets with credit guarantees. With a floor on potential losses established by the RCS, banks appear to be engaging in a "search for yield." After initially focusing on the relatively safer Manufacturing sector, competitive pressures and the pursuit of higher margins likely drove them to expand into segments like retail trade and miscellaneous services, which are often characterized by greater opacity, less tangible collateral, and higher inherent risk. The government guarantee is thus incentivizing a progressive movement down the credit quality curve over time. The risk profile of the guaranteed portfolio is not static; it appears to be deteriorating as banks test the boundaries of the scheme.

3. Risk Assessment of the Recent Borrower Surge (H1 2025)

The most pressing concern for the SME portfolio is the risk embedded within the massive and rapid influx of new, smaller-ticket borrowers during the first half of 2025. This section analyzes the specific sub-sectors where this surge has been concentrated and assesses the associated risk profile, which is heavily weighted towards working capital financing for less resilient business segments.

3.1. Analysis of Incremental Lending in Q2 2025

The trend towards smaller, more numerous loans accelerated significantly in the most recent quarter. Between March and June 2025, an additional 73,454 borrowers were added to the portfolio, while the total outstanding amount grew by PKR 103.1 billion. This implies an average ticket size for these new incremental loans of only PKR 1.40 million, a figure substantially lower than the overall portfolio average of PKR 2.50 million.

Sector	Mar-2025	Jun-2025	Incremental
Total Borrowers	203,139	276,593	+73,454
Total Outstanding (PKR mn)	658,491.7	761,576.8	+103,085.1
Average Ticket Size (PKR mn)	**2.88**	**2.50**	**1.40**

Data Source: NCGCL Memo, SBP Data Files

This sharp drop in the marginal ticket size confirms that the latest wave of lending is focused on much smaller enterprises, which inherently carry a higher risk profile due to greater vulnerability to economic shocks.

3.2. Identifying Influx Hotspots in Q2 2025

An estimation model allocating the 73,454 new borrowers in Q2 2025 reveals that the influx was highly concentrated in a few specific sub-sectors. The top three destinations—Other personal service activities, Wholesale trade (excluding motor vehicles), and Retail trade (excluding motor vehicles)—are estimated to have absorbed over 47,000 new borrowers, representing nearly 65% of the quarterly surge. The analysis also reveals the very small average loan size for these new entrants, particularly in the services and trade sectors.

ISIC Sub-sector Code & Description	Outstanding in Q2 2025 (PKR mn)	Estimated New Borrowers (Q2 2025)	Avg. Ticket Size of New Loans (PKR mn)
95 - Other personal service activities	658,491.7	17,030	1.40
46 - Wholesale trade (ex-motor)	21,345.1	15,201	1.40
47 - Retail trade (ex-motor)	21,085.4	15,016	1.40
01 - Agriculture & related	9,467.6	6,743	1.40
49 - Land transport & pipelines	4,112.1	2,929	1.41
41 - Construction of buildings	1,652.6	1,177	1.40

Data Source: NCGCL Memo, SBP Data Files

This granular view moves beyond broad sector categories to pinpoint the specific business activities where risk is accumulating most rapidly. The dominance of trade and personal services provides a clear target list for enhanced monitoring and supervisory attention.

3.3. Profile of High-Risk Segments

The risk profile of these hotspot segments is amplified by the nature of the financing being extended. The surge in borrowers has been accompanied by a decline in average ticket sizes and a heavy reliance on working capital loans. Critically, the majority of this new lending in Q2 2025 was extended on an unsecured or "clean" basis, with no tangible collateral. This dramatically increases the Loss Given Default (LGD) for this vintage, as recovery prospects in the event of default are minimal.

The sub-sector "95 - Other personal service activities" warrants particular concern. This category often includes businesses in the informal or quasi-formal economy, such as small repair shops and personal care services, which are characterized by volatile cash flows and minimal financial buffers. The influx of an estimated 21,132 new borrowers into this segment over six months, financed primarily through small, unsecured working capital loans, represents a significant accumulation of high-risk exposure.

Sub-sector	Estimated New Borrowers (H1 2025)	Working Capital (WC) Share of Financing	SME Share of Sector (Q2 2025)
46 - Wholesale trade (ex-motor)	203,139	72%	34%
95 - Other personal service activities	21,132	61%	55%
47 - Retail trade (ex-motor)	16,704	67%	41%

Data Source: NCGCL Memo, SBP Data Files

The RCS has enabled an unprecedented extension of formal credit into these traditionally underserved and higher-risk segments. While this aligns with the policy goal of financial inclusion, it introduces a systemic risk. Because thousands of these unsecured loans were underwritten in a short period under similar programmatic criteria, they are likely to exhibit highly correlated performance. A minor economic disruption could simultaneously impact this large, homogenous, and financially fragile cohort. Consequently, the Ministry should prepare for potential "waves" of non-performing loans (NPLs) and subsequent guarantee claims, triggered by events that affect these specific sub-sectors.

4. Portfolio Credit Risk Quantification

To translate the identified qualitative risks into actionable financial metrics, this section quantifies the potential credit losses for the entire SME portfolio. It establishes core risk parameters—Probability of Default (PD) and Loss Given Default (LGD)—and uses them to calculate the Expected Loss (EL) under various scenarios.

4.1. Probability of Default (PD) and Loss Given Default (LGD) Estimation

The estimation of core risk parameters is anchored in a blend of local performance data and insights from academic literature, providing a more robust basis for assessment.

Probability of Default (PD): While the observed Non-Performing Loan (NPL) ratio for the SME portfolio provides a useful, albeit backward-looking, anchor (approx. 15.4% in March 2025), it is not a direct proxy for the forward-looking Probability of Default. Academic studies on SME default rates in emerging markets suggest a wide range, with average default rates for private corporate lending typically falling between 3.6% and 6.3%. However, these studies often cover a broad mix of corporates.

Given the specific high-risk characteristics identified in Pakistan's recent SME loan vintage, namely, the influx of new, smaller, and less-documented businesses, adopting these lower international benchmarks would be imprudent. Therefore, a **base-case PD of 9.5%** is adopted.

This figure is adjusted downward from the historical NPL ratio to reflect the distinction between a stock measure (NPLs) and a forward-looking probability (PD), but remains elevated compared to global averages to account for the portfolio's deteriorating risk profile.

Loss Given Default (LGD): The LGD represents the portion of the loan that is not recovered after a default event. The shift towards unsecured lending in Q2 2025 necessitates a blended LGD approach for the total portfolio. For the legacy portfolio (up to March 2025), a **base-case LGD of 55%** is assumed, reflecting a mix of secured and unsecured lending. For the new vintage of predominantly clean loans added in Q2 2025, a much higher **LGD of 75%** is assumed due to the absence of collateral. This results in a blended **base-case LGD of 57.7%** for the entire portfolio as of June 2025.

4.2. Expected Loss (EL) Calculation

Using the established risk parameters, the Expected Loss for the entire PKR 761.6 billion SME portfolio as of June 2025 is calculated. The standard formula, EL=EAD×PD×LGD, where Exposure at Default (EAD) is the total outstanding loan amount, is applied across three scenarios to provide a robust range for fiscal planning and financial stability assessment.

- Base Case: This scenario uses the central estimates for PD and the blended LGD.
  EL = PKR 761,576.8 million × 9.5% × 57.7% = PKR 41,722 million
- Optimistic Case: This scenario assumes improved economic conditions, with a 20% reduction in the PD and a lower blended LGD of 47.7%.
  EL= PKR 761,576.8 million × (9.5% × 0.8) × 47.7% = PKR 27,612 million

- Stress Case: This scenario models an economic downturn, increasing the PD by 20% and raising the blended LGD to 67.7% to reflect suppressed recoveries on both legacy and unsecured loans.
EL= PKR 761,576.8 million × (9.5% × 1.2) × 67.7% = PKR 58,817 million

Scenario	PD Assumption	Blended LGD Assumption	Expected Loss (PKR mn)
Base Case	9.5%	57.7%	**41,722**
Optimistic	7.6%	47.7%	**27,612**
Stress	11.4%	67.7%	**58,817**

Data Source: EAD from SBP Data Files[1]; PD & LGD assumptions based on NCGCL Memo and academic literature

This table provides the Ministry with a financially quantified range of the total credit risk inherent in the national SME loan book. The base-case EL of PKR 41.7 billion represents a significant potential loss to the banking sector, underscoring the importance of the RCS as a stabilizing mechanism, but also highlighting the magnitude of the risk the government is now partially underwriting.

5. Fiscal Risk Outlook and RCS Claim Forecast

This section delivers the primary output for the Ministry of Finance: a forward-looking forecast of the direct budgetary impact from the Risk Coverage Scheme. The analysis isolates the RCS-eligible portion of the portfolio, calculates the Ministry's direct financial exposure, and projects potential government payouts under different economic scenarios.

5.1. Estimating the RCS-Eligible Portfolio (Exposure at Default)

The RCS applies only to fresh or incremental financing extended from July 1, 2024, onwards. Therefore, to forecast claims, it is necessary to first determine the size of this specific loan vintage. The Exposure at Default for the RCS-eligible portfolio (EAD_RCS) is calculated as the net growth in total SME financing from the scheme's inception date to the end of the analysis period.

- Outstanding SME Financing (June 30, 2025): PKR 761,576.8 million
- Outstanding SME Financing (June 30, 2024): PKR 574,572.3 million
- **EAD_RCS (Net Growth): PKR 187,004.5 million**

This PKR 187.0 billion represents the principal amount of new lending that is eligible for claims under the government guarantee over the first year of the scheme's operation.

5.2. Forecasting Ministry's Exposure and Guarantee Claims

The Ministry's direct financial exposure is determined by the first-loss coverage levels stipulated in the RCS: 20% for Small Enterprises (SEs) and 10% for Medium Enterprises (MEs). Assuming the new lending follows a 45% SE and 55% ME portfolio mix, the Ministry's maximum potential liability (the total first-loss amount guaranteed) is calculated as follows:

- EAD attributable to SEs (45% of EAD_RCS): PKR 84,152.0 million
- EAD attributable to MEs (55% of EAD_RCS): PKR 102,852.5 million
- **Ministry's First-Loss Exposure: (PKR 84,152.0 mn × 20%) + (PKR 102,852.5 mn × 10%) = PKR 27,115.7 million**

The forecast for guarantee claims is then derived by applying a forward-looking PD to this direct exposure. The stress scenario uses a higher PD to account for the significantly elevated risk profile of the RCS portfolio, over half of which consists of recent, unsecured loans.

$$\text{Expected Claim} = \text{Ministry's First Loss Exposure} \times \text{Forward PD}$$

Scenario	Forward PD Assumption	12-Month Expected Claims (PKR bn)
Central Case	8.5%	**2.30**
Prudent Stress Case	13.5%	**3.66**
Benign Case	6.0%	**1.63**

Data Source: EAD from SBP Data Files[1]; PD & LGD assumptions based on NCGCL Memo and academic literature

This forecast provides a direct and actionable input for the Ministry's budget process. While the central case projects a liability of PKR 2.30 billion, the prudent stress case suggests that claims could realistically reach PKR 3.66 billion. This higher stress estimate is directly attributable to the deteriorating quality of the new loan book, particularly the shift to high-LGD unsecured lending in the most recent quarter.

6. Data Integrity and Strategic Recommendations

Effective policy-making and risk management depend on the quality and granularity of available data. This final section highlights potential data integrity issues identified during the analysis and provides a set of strategic recommendations for the Ministry of Finance to enhance its oversight and manage the fiscal risks associated with the SME financing portfolio.

6.1. Identified Data Anomalies

The review of monthly sectoral data revealed several large and unexplained fluctuations, particularly in smaller sectors. These anomalous swings could indicate issues with data reporting, classification, or potentially concentrated, one-off lending activities that merit further investigation. Such data volatility can obscure underlying trends and affect the accuracy of risk modeling.

Dec 2023	Sector	MoM Δ (PKR mn)
Dec 2023	M. Administrative & support service activities	-1,940.3
Mar 2024	D. Electricity, gas, steam & air conditioning	+1,659.0
Aug 2024	D. Electricity, gas, steam & air conditioning	-1,538.1
Apr 2025	Q. Other services	+10,074.71
Jun 2025	F. Construction	+4,126.01
Jun 2025	Q. Other services	+10,513.8

Data Source: NCGCL Memo, SBP Data Files

The particularly large increases in "Other services" and "Construction" during H1 2025 align with the broader trend of expansion into these sectors but are of a magnitude that warrants verification with reporting institutions to ensure accuracy.

6.2. Strategic Recommendations

1. Adopt Tiered Budgeting for RCS Claims: There is a case to move beyond a single-point estimate for budgetary allocation. It is recommended to allocate a base budget corresponding to the central claim forecast of **PKR 2.30 billion.** In addition, a contingent reserve fund should be established to cover the prudently estimated stress scenario, providing a fiscal buffer up to **PKR 3.66 billion.** This approach ensures operational readiness while acknowledging the significant downside risk in the new portfolio.

2. Request Enhanced SBP Reporting for Vintage Analysis: The current aggregated data makes it impossible to distinguish the performance of the new, riskier loans from the seasoned legacy portfolio. The Ministry should formally engage with the SBP to request enhanced reporting from financial institutions that allows for "vintage analysis." This would involve tracking the NPL performance of the post-July 2024 loan cohort separately, with a specific data field for collateral status (secured vs. unsecured). Such data is critical for accurately recalibrating risk parameters and understanding the true risk being underwritten by the government guarantee.

3. Implement Targeted Sector and Collateral Monitoring: Given the heavy concentration of new, unsecured borrowers in specific sub-sectors, a generalized monitoring approach is insufficient. It is recommended to establish a joint task force with the SBP to conduct enhanced surveillance of the identified high-influx, high-risk segments. This should focus on **"95 - Other personal service activities," "47 - Retail trade,"** and "**46 - Wholesale trade."** Monitoring should include tracking early warning indicators such as delinquency rates (30+ days past due) and the proportion of new lending that is unsecured to provide a leading indicator of future NPLs and guarantee claims.

4. Initiate a Mid-Term Review of the RCS Incentive Structure: While the RCS has been highly effective at increasing credit volume, the analysis suggests it may be creating adverse selection by incentivizing high-volume, unsecured lending to the riskiest SME segments. The Ministry, in collaboration with the SBP, should plan a mid-term review of the scheme's parameters. This review could explore potential adjustments, such as tiered guarantee coverage based on collateral levels or the internal risk rating of the borrower, to better align the incentives of banks with prudent risk management and long-term portfolio sustainability.