The Pakistan Credit Rating Agency Limited

ENTITY RATINGS REPORT

PAKISTAN MICROFINANCE INVESTMENT COMPANY LIMITED

ENTITY	RATING	OUTLOOK	ACTION	DATE
Pakistan Microfinance Investment Company Limited (PMIC)	Long Term: AA Short Term: A1+	Stable	Initial	24th October, 2017

RATING RATIONALE

The ratings of Pakistan Microfinance Investment Company Limited (PMIC) take into account implicit support of the three sponsors, Pakistan Poverty Alleviation Fund (PPAF), Karandaaz Pakistan — funded by UK's Department for International Development (DFID) — and the KfW Development Bank, a German government-owned development bank. Considering the vital role of microfinance sector in Pakistan in enhancing financial inclusion, PMIC was established to build on the work undertaken by PPAF with lending operations of PPAF spun-off into PMIC. Licensed as a Non-Banking Financial Company by SECP, PMIC can attract funding from diversified sources and leverage its capital to enhance the scale of its impact. In addition to meeting the liquidity needs of the sector, which requires USD 3 bln to reach a target of 10 mln active clients by the year 2020, PMIC has also introduced Microfinance Plus services which contribute to its mission of providing broad-based services to its clients. Including the 20 MFIs, registered as NBMFIs under the SECP rules, and 11 MFBs currently licensed by SBP, PMIC's target market currently comprises 31 institutions. PMIC had a lending portfolio of ~ PKR 5.4bln disbursed among ~12 microfinance institutions as of Aug'17. Concentration of the portfolio would remain a key concern for credit management. The strong equity base (Aug'17: ~PKR 5.9bln) provides comfort to the assigned ratings. In addition to capital contribution from the sponsors, PMIC also has subordinate loans available from them, which reflects the sponsors' commitment to the institution's mission. Over the next 4 years, PMIC plans to expand its micro-finance lending portfolio to ~PKR 40 bln, with a fund base of ~ PKR 45bln, including equity and tier-2 capital of ~PKR 22bln. The board has been able to engage a management team of experienced professionals for the successful execution of the strategy, who have had lengthy association with the micro-finance sector in general and PPAF in particular.

The performance of the company will be monitored vis-à-vis the planned goals. With expansion of the lending portfolio, the company's ability to sustain the credit quality will also be tracked; use of rigorous control mechanism remains central to the company's performance and hence the ratings. Given the initial stage of operations, stability of the management team is integral for realization of business strategy.

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OCTOBER 2017

PAKISTAN MICROFINANCE INVESTMENT COMPANY (PMIC) PROFILE	
Incorporated	2016
Major business lines	▪ Provide funding (and other services) to microfinance providers, to promote financial inclusion in Pakistan and contribute to the sector's development.
Legal status	Un-Listed
Head Office	Islamabad

INDUSTRY SNAPSHOT

- MF sector crossed PKR 171 bln in loan portfolio with 5.2 mln borrowers as of Jun'17. Plans are to reach 10 mln borrowers by 2020, which requires ~PKR 300bln additional funding
- PMIC's target market currently comprises 20 MFIs, registered as NBMFIs with SECP, and 11 MFBs currently licensed by SBP
- The microfinance sector borrowing was ~PKR 54.7bln as of Dec'16; PMIC's lending book was ~PKR 5.4bln as of Aug'17

OWNERSHIP — STRONG

- Created by the Pakistan Poverty Alleviation Fund (PPAF) (49%) and Karandaaz Pakistan (38%) - funded by UK's Department for International Development (DFID) - and the KfW Development Bank (13%), a German government-owned development bank
- PPAF, in turn, is facilitated by support from the Government of Pakistan, The World Bank, International Fund for Agricultural Development (IFAD), KfW and other statutory and corporate donors. The lending operations of PPAF were spun-off into PMIC, that is monitoring PPAF's portfolio for a service fee during the transition, in addition to building its own lending operations
- Karandaaz Pakistan, established in August 2014, is supported by International development finance institutions, UK Department for International Development (UKAid) and the Bill & Melinda Gates Foundation
- KfW Development Bank is a German government-owned development bank, based in Frankfurt

GOVERNANCE — GOOD

- Seven members board, including two representatives of PPAF, one each of Kfw and Karandaaz and two Independent directors
- Board Chairman is Mr. Zubyr Soomro, a leading banker, carrying more than 36 years of experience in senior positions spread across various jurisdictions
- Board members carry vast experience in diversified sectors, providing adequate oversight to the company's operations
- Board has three sub-committees; i) Audit, ii) Human Resource and Remuneration and iii) Risk Committee, enabling effective oversight
- In-house Internal audit department developed and M/s KPMG Taseer Hadi & Co serves as external auditors

MANAGEMENT — GOOD

- Well-defined organizational structure, with four major department heads reporting to CEO
- Mr. Yasir Ashfaq, CEO of the company, carries an overall experience of more than 20 years at senior level positions. He previously served as the Group Head Financial Services Group at PPAF
- Key management personnel are qualified having diversified experience. Some of the senior management team members have had lengthy association with the micro-finance sector in general and PPAF in particular, which has provided stability to the organization. Given the initial stage of the company itself, continued stability and performance of the management team is integral for realization of business strategy
- Three management committees, i) Asset and Liability (ALCO), ii) Management Committee (MANCOM), and iii) Risk Committee, in place. Performance monitored and evaluated through periodic reports

RISK MANAGEMENT — GOOD

- Risk policies implemented in-line with the requirements of the SBP and SECP including criteria to measure, monitor and mitigate risk factors
- Cautious approach for lending with a multi-stage approval process. Internal Risk Rating System in place with ~40 indicators
- Considering risk profile and characteristics shared by the industry participants, it is classified into 6 categories; 2 for MFBs and 6 for MFIs
- Net lending to financial institutions amounts to total PKR 5.3 bln as at end-Aug'17. Exposures have been taken in line with Board approved policy for the institution's risk appetite, high concentration risk is emanating from 80% of lending portfolio deployed with five major institutions.
- Treasury will operate as a profit center, maintaining a portfolio of PKR 2-3bln. Funds would largely be invested in Commercial Banks rated "AAA" or in "AA" category and PIBs, and T-Bills

PERFORMANCE — GOOD

- Growing business led revenue to reach PKR 250mln in half year ended Jun'17 from only PKR 17mln in period ended Dec'16
- Service fee for handling PPAF's portfolio accounted for ~25% of gross revenues in half year ended Jun'17; this source of income is gradually being replaced by revenues on PMIC's own portfolio which the management has continued to build
- As PMIC is in start-up phase, administrative expenses are on the higher end (cost to revenue ratio of 47% for half year ended Jun'17). However, net income of PKR 64mln generated in half year ended Jun'17 relative to a loss of PKR 67mln in period ended Dec'16.
- Going forward, other operating income is expected to increase, providing additional cushion to bottom-line. PMIC plans to expand its portfolio to ~PKR 40bln by 2020
- A comprehensive business plan for 2017-2020 has been approved, entailing detailed timeline for rollout of planned initiatives

FINANCIAL RISK — GOOD

- Liquid assets (Jun17: PKR 3.4bln) provide comfortable cushion to the borrowings. With expansion in funding base, maintaining liquidity level remains central. Company intends to maintain 9-10% of its funds (equity plus borrowings) in liquid assets at all time.
- PMIC has available to it subordinate loans from sponsors, (PPAF: ~PKR 11.8bln, DFID / Karandaaz: ~ GBP 25 mln). As funding requirement increases, other commercial sources of funding will also be explored, including from commercial banks and Term Finance Certificate
- Current equity stands at PKR 5.9bln; the subordinate loan from PPAF (up to PKR 11.8bln) will contribute to Tier II capital. Internal capital generation is expected to improve as the business expands

Pakistan Microfinance Investment Company Limited PKR mln

BALANCE SHEET	30-Jun-17	31-Mar-17	Aug'16-Dec'16
	6M	3M	5M
Assets			
Lending to Financial Institutions			
1. Microfinance Institutions	4,159	1,350	-
2. Repurchase Agreement Lendings (Reverse REPO)	997	3,295	3,260
3. Others	-	-	-
	5,156	4,645	3,260
Other Earning Assets	2,326	1,010	2,350
Fixed Assets	26	11	3
Non-Earning Assets			
1. Cash and Bank Balances	104	122	257
2. Non-Performing Advances	-	-	-
3. Others	126	82	35
	7,737	**5,870**	**5,905**
Borrowings	1,818	-	-
Other Liabilities (Non-Interest Bearing)	39	14	88
Equity	5,881	5,856	5,817
Total Liabilities & Equity	**7,737**	**5,870**	**5,905**
INCOME STATEMENT			
Net Interest / Mark Up Revenue	245	116	17
Other Operating Income/Loss	7	2	17
Total Revenue	**252**	**118**	**34**
Administrative and General Expenses	(118)	(48)	(100)
Pre-provision Profit	**133**	**70**	**(66)**
Provisions	(42)	(14)	-
Pre-tax Profit	**91**	**57**	**(66)**
Net Income	**64**	**40**	**(67)**
Ratio Analysis			
Performance			
Cost-to-Total Revenue	47.0%	40.5%	295.8%
ROE	2.2%	2.7%	-1.2%
NIMR (Net Interest/Mark-up Revenue) / Total Assets	3.2%	2.0%	0.3%
Liquidity & Funding			
Liquid Assets / Deposits and Borrowings	188.5%	-	-
Finances / Total Assets	66.1%	78.9%	55.2%
Capital			
Equity / Total Assets	76.0%	99.8%	98.5%
Capital formation rate [Net Profit-dividends / Opening Equity] *	1.1%	0.7%	-1.1%

CREDIT RATING
SCALE & DEFINITIONS

Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

LONG TERM RATINGS

AAA	**Highest credit quality.** Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments.
AA+ AA AA-	**Very high credit quality.** Very low expectation of credit risk. Indicate very strong capacity for timely payment of financial commitments. This capacity is not significantly vulnerable to foreseeable events.
A+ A A-	**High credit quality.** Low expectation of credit risk. The capacity for timely payment of financial commitments is considered strong. This capacity may, nevertheless, be vulnerable to changes in circumstances or in economic conditions.
BBB+ BBB BBB-	**Good credit quality.** Currently a low expectation of credit risk. The capacity for timely payment of financial commitments is considered adequate, but adverse changes in circumstances and in economic conditions are more likely to impair this capacity.
BB+ BB BB-	**Moderate risk.** Possibility of credit risk developing. There is a possibility of credit risk developing, particularly as a result of adverse economic or business changes over time; however, business or financial alternatives may be available to allow financial commitments to be met.
B+ B B-	**High credit risk.** A limited margin of safety remains against credit risk. Financial commitments are currently being met; however, capacity for continued payment is contingent upon a sustained, favorable business and economic environment.
CCC CC C	**Very high credit risk.** Substantial credit risk "CCC" Default is a real possibility. Capacity for meeting financial commitments is solely reliant upon sustained, favorable business or economic developments. "CC" Rating indicates that default of some kind appears probable. "C" Ratings signal imminent default.
D	Obligations are currently in default.

SHORT TERM RATINGS

A1+: The highest capacity for timely repayment.

A1:. A strong capacity for timely repayment.

A2: A satisfactory capacity for timely repayment. This may be susceptible to adverse changes in business, economic, or financial conditions.

A3: An adequate capacity for timely repayment. Such capacity is susceptible to adverse changes in business, economic, or financial conditions.

B: The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions.

C: An inadequate capacity to ensure timely repayment.

Outlook (Stable, Positive, Negative, Developing)
Indicates the potential and direction of a rating over the intermediate term in response to trends in economic and/or fundamental business/financial conditions. It is not necessarily a precursor to a rating change. 'Stable' outlook means a rating is not likely to change. 'Positive' means it may be raised. 'Negative' means it may be lowered. Where the trends have conflicting elements, the outlook may be described as 'Developing'.

Rating Watch
Alerts to the possibility of a rating change subsequent to, or in anticipation of, a) some material identifiable event and/or b) deviation from expected trend. But it does not mean that a rating change is inevitable. A watch should be resolved within foreseeable future, but may continue if underlying circumstances are not settled. Rating Watch may accompany Outlook of the respective opinion.

Suspension
It is not possible to update an opinion due to lack of requisite information. Opinion should be resumed in foreseeable future. However, if this does not happen within six (6) months, the rating should be considered withdrawn.

Withdrawn
A rating is withdrawn on a) termination of rating mandate, b) cessation of underlying entity, c) the debt instrument is redeemed, d) the rating remains suspended for six months, e) the entity/issuer defaults., or/and f) PACRA finds it impractical to surveill the opinion due to lack of requisite information

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Regulatory and Supplementary Disclosure

Name of Issuer Pakistan Microfinance Investment Company Limited
Sector Microfinance
Type of Relationship Solicited

Purpose of the Rating Independent Risk Assessment

Rating History

Dissemination Date	Long Term	Short Term	Outlook	Action
24-Oct-17	AA	A1+	Stable	Initial

Related Criteria and Research

Rating Methodology
Methodology | Non-Banking Finance Companies (Jan 17)
Methodology | MicroFinance Institutions (Jun 17)
Methodology | Bank Rating (Jun 17)

Sector Research
Sector Study | DFIs | Oct-17

Rating Analysts
Mahina Majid
mahina.majid@pacra.com
(92-42-35869504)

Rating Team Statement

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Probability of Default (PD)

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