The Pakistan Credit Rating Agency Limited

APNA MICROFINANCE BANK LIMITED

	NEW [APR-16]	PREVIOUS [APR-15]
Entity		
Long Term	BBB+	BBB+
Short Term	A3	A3
Outlook	Positive	Stable

REPORT CONTENTS

APRIL 2016

Profile & Ownership

- Incorporated in May03, Apna Bank had been operating as provincial microfinance bank till the grant of National level license in May15
- The bank operates with 69 branches (Punjab: 31, Sindh: 30, KPK: 5, Baluchistan: 1, AJK: 1, Gilgit: 1) across the country at end-Dec15
- Majorly owned (43%) by United International Group (UIG) through United Insurance Company (38%) and Mian Akram Shahid (5%), the founder and the Group Chairman

Governance

- Board comprises seven members; all shareholders of the bank including one executive member – the President and CEO
- Presently no independent director on the board, as against requirement of two under the MFBs Prudential Regulations; likely changes in board size to achieve regulatory compliance in upcoming board election in Jun16

Management

- Mr. Farooq Abid Tung, appointed as the President and CEO in Apr15, has been with the bank since 2013, carries extensive experience in financial sector
- High management turnover; during CY15, six changes were witnessed at the top-tier
- Adequately experienced management team, though relatively new to the bank

Risk Management

- AutoBANKER-II, a core-banking software, implemented
- Loan Book grew significantly during CY15 (end-Dec15: PKR 2,535mln, end-Dec14: PKR 697mln) with notable concentration (85%) in single product
- Secured loans constitute 12% of total advances
- Owing to hefty rise in loan base, the bank’s infection ratio reduced (Dec15: ~5%, Dec14: ~13%), though remained significantly higher than the industry

Performance

- During CY15, earning assets witnessed manifold growth to stand at PKR 4.5bln at end-Dec15) mainly on the back of advances (net addition PKR ~2bln). Spread notably declined during the year (CY15: 8.7%, CY14: 11.6%).
- Owing to expansion in branch network, the bank’s cost-to-total revenue ratio increased (CY15: 98%, CY14: 86%)
- The bank made a net loss of PKR 29mln (CY14: profit of PKR 6mln) in CY15
- Investment portfolio, PKR 227mln (22% of equity base), majorly comprises government securities (86%) (T-bills: PKR 141mln, PIBs: PKR 54mln) followed by investment in fixed income mutual fund (14%).
- Management is aggressively pursuing expansion; 51 new braches to be opened by end-Dec16. Resultantly, business volumes are expected to increase
- Effective implementation of business strategy and building a cohesive management team remains critical.

Financial Risk

- Apna bank solely relies on deposits as its funding source. During CY15, the bank aggressively mobilized deposits with net addition of PKR 3.4bln to stand at PKR 4.5bln at end-Dec15
- Liquidity profile remained healthy as reflected by liquid-assets-to-deposits and borrowings ratio of 48% at end-Dec15 (end-Dec14: 65%); though reduced on YoY basis
- The bank increased its paid-up capital (end-Dec15: PKR 1,250mln, end-Dec14: PKR 700mln) through 100% right issue during 2QCY15 strengthening risk absorption capacity of the bank. CAR declined from 48% at end-Dec14 to ~30% at end-Dec15; a factor of increase in lending portfolio; however remains adequate.

RATING RATIONALE

Apna Bank's ratings reflect the sponsors' demonstrated commitment in providing requisite support - right issue (PKR 550mln) has been completed and the bank has obtained National license (May15) to operate country wide. This, while providing larger operating platform, gives the requisite cushion to risk absorption capacity. Since, May15, notable changes have been witnessed in Apna's business strategy encompassing (i) shifting of Head Office to Punjab - core geography of the sponsors, (ii) rapid expansion mainly in Punjab; 40 new branches opened in 2HCY15, and (iii) strengthening management team. The ensuing benefit is significant build-up of deposit base. Meanwhile, the bank has increased its lending portfolio. Thus achieving good asset quality - currently portfolio at risk is relatively higher than sector norm - both for existing and new disbursements is a key challenge; though expected to rationalize due to geographic change. With on-going branch expansion, operational costs are mounting; these are expected to remain high in CY16. However, the management is eyeing operational profit in CY16 benefiting from increasing business volumes. Strengthening of governance framework and related systems & controls to support expansion remains important.

'Positive Outlook' is assigned to the ratings incorporating improved equity base and subsequent grant of National level license. This should help the bank to improve its market position besides strengthening its standalone profile.

KEY RATING DRIVERS

While effective management of transition is important, achievement of operational profit on sustainable basis along with strong asset quality - at par with industry - are requisites for rating upgrade. Meanwhile, board composition in line with regulatory compliance for better governance and team cohesiveness are also important.

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Apna Microfinance Bank Limited

PKR mln

BALANCE SHEET	31-Dec-15	31-Dec-14	31-Dec-13
Earning Assets			
Total Finances	2,566	747	330
Investments	227	141	211
Deposits with Banks	1,709	518	505
	4,502	**1,406**	**1,046**
Non Earning Assets			
Non-Earning Cash	287	78	63
Net Non-Performing Finances	53	69	69
Fixed Assets & Others	828	206	136
	1,168	**353**	**267**
TOTAL ASSETS	**5,670**	**1,759**	**1,313**
Interest Bearning Liabilities			
Deposits			
CASA	2437	500	379
Time Deposits	2110	694	383
	4547	1,194	762
Non Interest Bearing Liabilities	69	23	34
TOTAL LIABILITIES	**4,615**	**1,216**	**796**
EQUITY (including revaluation surplus)	**1030**	**511**	**505**
Deferred Grants	**25**	**32**	**12**
TOTAL LIABILITIES & EQUITY	**5,670**	**1,759**	**1,313**

INCOME STATEMENT	31-Dec-15	31-Dec-14	31-Dec-13
	Annual	Annual	Annual
Interest / Mark up Earned	447	239	139
Interest / Mark up Expensed	187	(79)	(52)
Net Interest / Markup revenue	**635**	**160**	**87**
Other Operating Income	40	10	6
Total Revenue	**675**	**170**	**93**
Other Income	57	24	9
Non-Interest / Non-Mark up Expensed	(352)	(166)	(125)
Pre-provision operating profit	381	28	(23)
Provisions	(30)	(20)	(30)
Pre-tax profit	351	9	(52)
Taxes	(5)	(3)	(1)
NET INCOME	**346**	**6**	**(53)**

Ratio Analysis	31-Dec-15	31-Dec-14	31-Dec-13
Performance			
ROE	-2.8%	1.2%	-13.1%
Cost-to-Total Net Revenue	98.4%	85.4%	122.1%
Capital Adequacy			
Equity/Total Assets	18.2%	29.0%	38.6%
Capital Adequacy Ratio as per SBP	29.8%	48.0%	81.0%
Loan Loss Coverage			
Non-Performing Advances /Gross Advances	4.5%	12.7%	26.8%
Loan Loss Provisions / Non-Performing Advances	55.3%	32.1%	24.9%
Funding & Liquidity			
Liquid Assets / Deposits and Borrowings	48.6%	65.1%	109.9%
Advances / Deposits	59.1%	71.1%	55.4%
CASA deposits / Total Customer Deposits	53.6%	41.9%	50.0%
Intermediation Efficiency			
Asset Yield	16.1%	19.8%	17.2%
Cost of Funds	7.4%	8.2%	8.5%
Spread	8.7%	11.6%	8.7%
Outreach			
Branches	69	17	11

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STANDARD 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. This capacity is highly unlikely to be adversely affected by foreseeable events.
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-**	**Speculative.** Possibility of credit risk developing. There is a possibility of credit risk developing, particularly as a result of adverse economic change over time; however, business or financial alternatives may be available to allow financial commitments to be met.
B+ **B** **B-**	**Highly speculative.** Significant 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**	**High default 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.

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. Rating Watch may carry designation – Positive (rating may be raised, negative (lowered), or developing (direction is unclear). A watch should be resolved with in foreseeable future, but may continue if underlying circumstances are not settled.

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'.

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, or e) the entity/issuer defaults.

Regulatory and Supplementary Disclosure

Name of Issuer	Apna Microfinance Bank Limited
Sector	Microfinance
Type of Relationship	Solicited
Purpose of the Rating	Independent Risk Assessment

Rating History

Dissemination Date	Long Term	Short Term	Outlook	Action
07-Apr-16	BBB+	A3	Positive	Maintained
07-Apr-15	BBB+	A3	Stable	Upgrade
12-May-14	BBB	A3	Positive	Maintained
15-May-13	BBB	A3	Positive	Maintained
30-Apr-12	BBB	A3	Positive	Maintained

Related Criteria and Research

Rating Methodology: Microfinance Institution

Sector Research: Microfinance | Viewpoint | Mar-16

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Rating Team Statement

Rating Procedure
Rating is an opinion on relative credit worthiness of an entity or debt instrument. It does not constitute recommendation to buy, hold or sell any security. The rating team for this assignment does not have any beneficial interest, direct or indirect in the rated entity/instrument.

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Rating Shopping
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PACRA may provide consultancy/advisory services or other services to any of its clients or to any of its clients' associated companies and associated undertakings that is being rated or has been rated by it. In such cases, PACRA has adequate mechanism in place ensuring that provision of such services does not lead to a conflict of interest situation with its rating activities
PACRA receives compensation from the entity being rated or any third party for the rating services it offers. The receipt of this compensation has no influence on PACRA's opinions or other analytical processes. In all instances, PACRA is committed to preserving the objectivity, integrity and independence of its ratings. Our relationship is governed by two distinct mandates i) rating mandate - signed with the entity being rated or issuer of the debt instrument, and ii) fee mandate - signed with the payer, which can be different from the entity
PACRA ensures that the credit rating assigned to an entity or instrument should not be affected by the existence of a business relationship between PACRA and the entity or any other party, or the non-existence of such a relationship

Surveillance
PACRA monitors all the outstanding ratings continuously and any potential change therein due to any event associated with the rated entity/ issuer, the security arrangement, the industry etc, is disseminated to the market, in a timely and effective manner, after appropriate consultation with the entity/issuer
PACRA reviews all the outstanding ratings on annual basis or as and when required by any stakeholder (including creditor) or upon the occurrence of such an event which requires to do so
PACRA initiates immediate review of the outstanding rating(s) upon becoming aware of any information that may be reasonable be expected to result in any change (including downgrade) in the rating

Reporting of Misconduct
PACRA has framed and implemented whistle-blower policy encouraging all employees to intimate the compliance officer any unethical practice or misconduct relating to the credit rating by another employees of the company that came to his/her knowledge. The Compliance Officer reports to the BoD and SECP

Confidentiality
PACRA has framed a confidentiality policy to prevent abuse of the non-public information by its employees and other persons involved in the rating process, sharing and dissemination of the non-public information by such persons to outside parties
Where feasible and appropriate, prior to issuing or revising a rating, PACRA informs the issuer of the critical information and principal considerations upon which a rating will be based and provide the opportunity to clarify any likely factual misperception or other matter that PACRA would wish to be made aware of in order to produce a fair rating. PACRA duly evaluates the response. Where in a particular circumstance PACRA has not informed the entity/issuer prior to issuing or revising a rating, it informs the entity/issuer as soon as practical thereafter

Prohibition

Probability of Default (PD)

PACRA's Rating Scale reflects the expectation of credit risk. The highest rating has the lowest relative likelihood of default (i.e, probability). PACRA's transition studies capture the historical performance behavior of a specific rating notch. Transition behavior of the assigned rating can be obtained from PACRA's Transition Study available at our website. (www.pacra.com). However, actual transition of rating may not follow the pattern observed in the past