The Pakistan Credit Rating Agency Limited

Rating Report

GuarantCo Limited

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
27-Jun-2023	AAA	A1+	Stable	Maintain	-
30-Jun-2022	AAA	A1+	Stable	Maintain	-
30-Jun-2021	AAA	A1+	Stable	Maintain	-
30-Jun-2020	AAA	A1+	Stable	Maintain	-
28-Dec-2019	AAA	A1+	Stable	Maintain	-
28-Jun-2019	AAA	A1+	Stable	Maintain	-
31-Dec-2018	AAA	A1+	Stable	Maintain	-
18-May-2018	AAA	A1+	Stable	Maintain	-
29-Sep-2017	AAA	A1+	Stable	Maintain	-

Rating Rationale and Key Rating Drivers

GuarantCo Limited, an international Joint Venture development financial institution, is the local currency guarantee arm of the Private Infrastructure Development Group (PIDG). It is directly and indirectly owned by five highly-rated sovereigns. Support of the sponsors is evident from time to time in the form of injection of capital. GuarantCo mainly operates in low-income, below-investment-grade countries as per its mandate. Currently, the exposure is in eighteen countries wherein, most of the exposure lies in corporate finance & project finance. There is increased focus towards Asia from Africa evident from the enhanced portfolio in the South Asian market. The emerging Asian market is representing around 50% of the portfolio. The current portfolio is skewed towards energy, transport, and inputs for infrastructure, telecom, and urban infrastructure sectors. Asset quality remains a major concern as pressures are building up in key markets as South Asia has been hit by a series of unique challenges, including inflation, and global economic slowdown. Growth remained slow in mid-22, although economies driven by services fared better. During CY22, guarantee income recorded a slight downtick while other income from the portfolio increased. Net loss from portfolio declined YoY in CY22. Liquidity indicators remained in a good range.

GuarantCo Management Company, a fully owned subsidiary of Cardano Development, is the fund manager responsible for GuarantCo's commercial operations. GuarantCo's ratings are dependent on its robust ownership structure & strong liquidity buffer. Prudent expansion and close monitoring of asset quality and internal obligor rating remain critical.

Disclosure

Name of Rated Entity	GuarantCo Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology | Correlation Between Long-term & Short-term Rating Scales(Jun-22),Methodology | Rating Modifiers(Jun-22),Methodology | Non-Banking Finance Companies Rating(Jun-22)
Related Research	Sector Study | Credit Guarantee Institutions(Jun-22)
Rating Analysts	Sehar Fatima | sehar.fatima@pacra.com | +92-42-35869504

Profile

Structure GuarantCo Limited (GuarantCo) was incorporated in Port Louis, Mauritius on August 25, 2005 as an unlisted company.

Background GuarantCo is a Joint Venture Financial Institution with international operations. GuarantCo's registered office is located in Mauritius.

Operations The key objectives of establishing the entity are to, i) support infrastructure projects in low-income countries via guarantee provisions which in turn, enable the said projects to raise debt financing and, ii) development of local financial debt markets. Thus, GuarantCo facilitates to bridge the funding gap that the local debt market would fail to meet due to capacity constraints, exposure limits and other covenants.

Ownership

Ownership Structure The ultimate ownership of GuarantCo lies with five governments United Kingdom, Netherlands, Sweden, Switzerland, and Australia. Shareholders are five highly rated sovereigns - United Kingdom (AA- by Fitch), Switzerland (AAA by Fitch), Sweden (AAA by Fitch), Netherlands (AAA by Fitch), and Australia (AAA by S&P). With the exception of the Netherlands Development Finance Company (FMO), which contributes 11% of GuarantCo's total paid-in capital, the agencies act jointly under the umbrella of the Private Infrastructure Development Group (PIDG). GuarantCo also has stand-by debt facilities made available by non-shareholding sponsors such as the AFD and the government of Canada.

Stability The company's ownership structure is expected to remain the same in the foreseeable future.

Business Acumen The business acumen is considered strong as PIDG and FMO are associated with same business.

Financial Strength PIDG with consolidated strength of eight members is a donor-financed trust while FMO is a development bank (51% owned by the Dutch government through the Dutch Ministry of Foreign Affairs). Capital injections by sponsors on a continuous basis signify a commitment to support. Although no formal commitment exists, the likelihood of support from the sponsors is high in case of need.

Governance

Board Structure GuarantCo's five-member BOD comprises of non-executive directors - qualified professionals with emerging and frontier market experience.

Members' Profile Ms. Yukiko Omura is serving the board as chairman since 2018 and carries more than three decades of experience in multilateral development agencies and leading investment banks.

Board Effectiveness Effectiveness Since CY 18, all sub-board committees' functions have been delegated to PIDG for the smooth functioning of operations.

Financial Transparency The Company's auditors, Binder Dijker Otte (BDO), are among the well-reputed audit firms internationally.

Management

Organizational Structure Management of guarantee portfolio is outsourced to GuarantCo Management Company Limited (GMCL), a fully owned subsidiary of Cardano Development. Treasury investment book is subcontracted to PIMCO and Fidelity.

Management Team Mr. Layth Al-Falaki (CRO at PIDG and Non-Executive Director on the Emerging Africa Infrastructure Fund's boards) has been appointed as Chief Executive Officer of GuarantCo. Mr. Falaki has assumed his office since mid-January 2022. The entire reporting line of GuarantCo terminates into CEO. The entire management team consists of five Executive Officers, who carry extensive experience which bodes well for the risk profile of the company.

Effectiveness On May 9, 2016, GuarantCo Management Company Limited (GMC) took over the management agreement from Frontier Markets Fund Manager Limited (FMFML) - the manager of GuarantCo since 2006. GMC is a 100% subsidiary of Cardano Development. The scope of GMC's core responsibilities is to; identify new business opportunities ensure compliance with related policies, make business plans and budget; perform due diligence and negotiate arrangements for new guarantees to be initiated; and continuously review and manage of business portfolio and guarantee products.

MIS Various manuals and policies have been put in place by the PIDG to overlook all management functions.

Risk Management Framework RMF comprehensively covers; i) measurement tools/models (Project rating model), ii) establishment of limits (guarantees, investments), and iii) policies and procedural manuals related to overall risk management. RMF has developed Guarantee Policy and operational guidelines which covers credit, market, liquidity and operational risks and will be consistent with PIDG operational policies and procedures.

Business Risk

Industry Dynamics Credit Guarantee Institutions (CGIs) facilitate lending by providing credit guarantees against the risk of default of issuers. These guarantees help these entities in raising debt from financial institutions. Thus, CGIs are vital source of financial assistance to these entities. Globally, most CGIs are mandated to promote business, financial markets and infrastructure development activities mainly in less developed segments.

Relative Position GuarantCo is a specialized financial guarantor. It issues guarantees to enhance the credit quality of debt instruments, mainly loans and bonds issued in local currency to finance infrastructure projects in emerging markets.

Revenues GuarantCo's revenue source comprises two main streams: (i) guarantee income (fees received from its clients on the committed guarantees) and (ii) income on its investment portfolio. Revenue is also received from interest on funded exposures. During CY22, guarantee revenue slightly dipped by 2% (CY22: USD 12.2mln; CY21: USD 12.5mln). Moreover, net investment income also recorded a loss of USD 3.4mln (Loss in CY21: USD 0.341mln).

Performance GuarantCo reported a loss after tax of USD 26.7mln (CY21: USD 55.1mln). The loss is primarily due to loan receivables impairments and adjustments for credit risk.

Sustainability GCL's portfolio has a major weight of guarantees/exposures in South Asia as per mandate, specifically towards India and Pakistan. The company has been aiming to expand its guarantee portfolio in upcoming years.

Financial Risk

Credit Risk The current portfolio is spread across more than eighteen countries and twelve sectors. The current guarantee portfolio size as of end-Dec'22 stood at USD 1,008mln (EndDec21: USD 882.7mln), showing an upward trend. As at end-Dec'22, the company's country-wise exposure is concentrated towards India (24%) followed by Vietnam (11.7%) and Pakistan (7%).

Market Risk The investment portfolio remained stagnant as it stood at USD 119mln (CY21: USD 125.4mln). The investment book of the company constitutes 44.5% of the total asset base and is dominated primarily by derivative financial instruments at FVTPL.

Liquidity And Funding The liquidity profile slightly declined during the period under review reflected in the liquidity ratio for CY22 stated as 207.9% (CY21: 243.0%).

Capitalization The company possesses a sound capitalization level as evidenced by healthy capital to guarantee portfolio reporting 352 times as at end-Dec'22 (end-Dec' 21: 107.8 times). The Company's Shareholders' equity ratio reported at 83.7% as at end-Dec'22 is fairly adequate (end-Dec' 21: 69.4%).

GuarantCo Limited

	31-Dec-22	31-Dec-21	31-Dec-20
Balance Sheet	*Annual*	*Annual*	*Annual*
ASSETS			
Earning Assets			
1. Deposits with Banks	131,378	186,493	169,233
2. Investments	119,950	125,377	130,328
3. Gaurantee Contracts	978	2,989	4,119
Trade and other receivables	15,555	15,022	17,754
Deferred expenses	790	569	295
Deferred Tax	432	432	-
TOTAL ASSETS	**269,083**	**330,883**	**321,729**
LIABILITIES			
Current Liabilities			
1. Derivative Financial Instruments	81	166	203
2. Financial Guarantee Contracts & Facility Agreements FVTPL	4,331	62,683	30,451
3. Trade and other payables	38,310	36,989	5,436
4. Provision - Guarantee payable	(6,511)	-	-
Other Liabilities	1,220	1,272	1,776
EQUITY			
TOTAL EQUITY	225,141	229,773	279,744
TOTAL LIABILITIES & EQUITY	**262,572**	**330,883**	**317,610**

INCOME STATEMENT

	31-Dec-22	31-Dec-21	31-Dec-20
Portfolio Revenue - Net	(2,466)	(36,324)	11,832
Finance Income	(3,405)	(341)	7,715
Fund Manager Fee & Administrative expenses	(20,864)	(18,403)	(16,963)
Profit Before Taxation	(26,734)	(55,068)	2,583
Taxation	-	(48)	(459)
Net Income	**(26,734)**	**(55,116)**	**2,124**

RATIO ANALYSIS

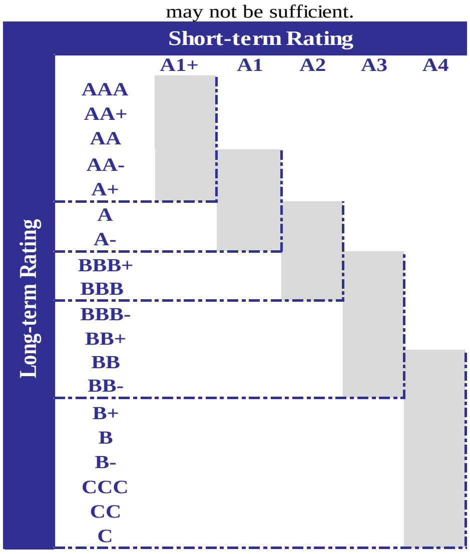
	31-Dec-22	31-Dec-21	31-Dec-20
Profitability Ratios			
1. ROE	-23.7%	-48.0%	1.5%
Liquidity Ratios			
1. Liquid Assets/Gross Guarantees	207.9%	243.0%	222.8%
2. Liquid Assets/Equity	58.4%	81.2%	60.5%
Capital Adequacy			
1. Equity/Total Assets	83.7%	69.4%	88.1%
2. Equity/Gross Guarantees	186.2%	179.0%	208.1%

Credit Rating

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 Rating	
Scale	**Definition**
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 Rating	
Scale	**Definition**
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
A4	The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions. Liquidity may not be sufficient.



**The correlation shown is indicative and, in certain cases, may not hold.*

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 some material identifiable event with indeterminable rating implications. 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 rating 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) the debt instrument is redeemed, c) the rating remains suspended for six months, d) the entity/issuer defaults., or/and e) PACRA finds it impractical to surveill the opinion due to lack of requisite information.

Harmonization A change in rating due to revision in applicable methodology or underlying scale.

Surveillance. Surveillance on a publicly disseminated rating opinion is carried out on an ongoing basis till it is formally suspended or withdrawn. A comprehensive surveillance of rating opinion is carried out at least once every six months. However, a rating opinion may be reviewed in the intervening period if it is necessitated by any material happening.

Note. This scale is applicable to the following methodology(s):

a) Broker Entity Rating
b) Corporate Rating
c) Debt Instrument Rating
d) Financial Institution Rating
e) Holding Company Rating
f) Independent Power Producer Rating
g) Microfinance Institution Rating
h) Non-Banking Finance Companies Rating

Regulatory and Supplementary Disclosure
(Credit Rating Companies Regulations,2016)

Rating Team Statements
(1) Rating is just an opinion about the creditworthiness of the entity and does not constitute recommendation to buy, hold or sell any security of the entity rated or to buy, hold or sell the security rated, as the case may be | Chapter III; 14-3-(x)

2) **Conflict of Interest**
i. The Rating Team or any of their family members have no interest in this rating | Chapter III; 12-2-(j)
ii. PACRA, the analysts involved in the rating process and members of its rating committee, and their family members, do not have any conflict of interest relating to the rating done by them | Chapter III; 12-2-(e) & (k)
iii. The analyst is not a substantial shareholder of the customer being rated by PACRA [Annexure F; d-(ii)] Explanation: for the purpose of above clause, the term "family members" shall include only those family members who are dependent on the analyst and members of the rating committee

Restrictions
(3) No director, officer or employee of PACRA communicates the information, acquired by him for use for rating purposes, to any other person except where required under law to do so. | Chapter III; 10-(5)
(4) PACRA does not disclose or discuss with outside parties or make improper use of the non-public information which has come to its knowledge during business relationship with the customer | Chapter III; 10-7-(d)
(5) PACRA does not make proposals or recommendations regarding the activities of rated entities that could impact a credit rating of entity subject to rating | Chapter III; 10-7-(k)

Conduct of Business
(6) PACRA fulfills its obligations in a fair, efficient, transparent and ethical manner and renders high standards of services in performing its functions and obligations; | Chapter III; 11-A-(a)
(7) PACRA uses due care in preparation of this Rating Report. Our information has been obtained from sources we consider to be reliable but its accuracy or completeness is not guaranteed. PACRA does not, in every instance, independently verifies or validates information received in the rating process or in preparing this Rating Report | Clause 11-(A)(p).
(8) PACRA prohibits its employees and analysts from soliciting money, gifts or favors from anyone with whom PACRA conducts business | Chapter III; 11-A-(q)
(9) PACRA ensures before commencement of the rating process that an analyst or employee has not had a recent employment or other significant business or personal relationship with the rated entity that may cause or may be perceived as causing a conflict of interest; | Chapter III; 11-A-(r)
(10) PACRA maintains principal of integrity in seeking rating business | Chapter III; 11-A-(u)
(11) PACRA promptly investigates, in the event of a misconduct or a breach of the policies, procedures and controls, and takes appropriate steps to rectify any weaknesses to prevent any recurrence along with suitable punitive action against the responsible employee(s) | Chapter III; 11-B-(m)

Independence & Conflict of interest
(12) 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 fee mandate - signed with the payer, which can be different from the entity
(13) PACRA does not provide consultancy/advisory services or other services to any of its customers or to any of its customers' associated companies and associated undertakings that is being rated or has been rated by it during the preceding three years unless it has adequate mechanism in place ensuring that provision of such services does not lead to a conflict of interest situation with its rating activities; | Chapter III; 12-2-(d)
(14) PACRA discloses that no shareholder directly or indirectly holding 10% or more of the share capital of PACRA also holds directly or indirectly 10% or more of the share capital of the entity which is subject to rating or the entity which issued the instrument subject to rating by PACRA; | Reference Chapter III; 12-2-(f)
(15) PACRA ensures that the rating assigned to an entity or instrument is 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 | Chapter III; 12-2-(i)
(16) PACRA ensures that the analysts or any of their family members shall not buy or sell or engage in any transaction in any security which falls in the analyst's area of primary analytical responsibility. This clause shall, however, not be applicable on investment in securities through collective investment schemes. | Chapter III; 12-2-(l)
(17) PACRA has established policies and procedure governing investments and trading in securities by its employees and for monitoring the same to prevent insider trading, market manipulation or any other market abuse | Chapter III; 11-B-(g)

Monitoring and review
(18) PACRA monitors all the outstanding ratings continuously and any potential change therein due to any event associated with the issuer, the security arrangement, the industry etc., is disseminated to the market, immediately and in effective manner, after appropriate consultation with the entity/issuer; | Chapter III | 18-(a)
(19) PACRA reviews all the outstanding ratings on semi-annual basis or as and when required by any creditor or upon the occurrence of such an event which requires to do so; | Chapter III | 18-(b)
(20) PACRA initiates immediate review of the outstanding rating upon becoming aware of any information that may reasonably be expected to result in downgrading of the rating; | Chapter III | 18-(c)
(21) PACRA engages with the issuer and the debt securities trustee, to remain updated on all information pertaining to the rating of the entity/instrument; | Chapter III | 18-(d)
Probability of Default
(22) 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 | Chapter III | 14-(f-VII)
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