



The Pakistan Credit Rating Agency Limited

Rating Report

NRSP Microfinance Bank Limited

Report Contents

1. Rating Analysis
2. Financial Information
3. Rating Scale
4. Regulatory and Supplementary Disclosure

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
06-Nov-2018	A	A1	Stable	Maintain	-
30-Apr-2018	A	A1	Stable	Maintain	-
31-Oct-2017	A	A1	Stable	Maintain	-
29-Apr-2017	A	A1	Stable	Initial	-

Rating Rationale and Key Rating Drivers

The ratings incorporate the bank's notable position in the microfinance sector, evident from its ~10% share in MFBs' gross loan portfolio and ~12% in the MFBs' deposits. The design of lending product keeps the concentration high wherein a sizable portion of the loan book is dedicated to crop-linked loans, particularly to sugarcane crops. The bank's asset quality reflects a deteriorated position (Infection ratio; ~4.1%) as sugarcane industry encountered adversities resulting in backlog of payments to sugarcane farmers. Short-term strategy, therefore, remains focal to consolidating the interrupted position, including dilution of the loan book concentration. The bank's financial risk profile is reflected by sanguine margins and average growth in loan portfolio. Funding base majorly accounts for deposits constituting a high chunk of time deposits. The ratings take comfort from association of NRSP Microfinance Bank with the National Rural Support Programme, the major shareholder, and with the three foreign development organizations - IFC, Acumen, and KfW, providing both technical and financial support to the bank. Focus on poverty alleviation for the underprivileged community remains pivotal in modelling the bank's strategy.

The ratings are dependent on the bank's ability to sustain its competitive position in the MFBs market. Reviving asset health is critical. Meanwhile, prudent management of liquidity profile alongside strengthening of capital base remain imperative.

Disclosure

Name of Rated Entity	NRSP Microfinance Bank Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology Criteria Rating Modifier(Jun-18),Methodology Correlation Between Long-Term And Short-Term Rating Scale(Jun-18),Methodology MFI (Jun-18)
Related Research	Sector Study Microfinance Bank(Apr-18)
Rating Analysts	Nadeem Sheikh nadeem.sheikh@pacra.com +92-42-35869504

The Pakistan Credit Rating Agency Limited

Profile

Structure NRSP Microfinance Bank Limited ("the Bank") was incorporated as a public unlisted company in October 2008 under Section 32 of the Companies Ordinance, 1984 (now Companies Act, 2017). The Bank commenced operations in March-2011 as a nationwide microfinance bank.

Background The bank builds on the experience of its parent institution - National Rural Support Programme (NRSP) which in 2008, spun-off its Micro Enterprise Development Programme (MEDP) into a separate bank – NRSP Microfinance Bank with an existing portfolio of ~165,000 clients; this kicked-off a solid start for the bank.

Operations The bank currently operates with a nationwide network of 121 branches with its head office in Bahawalpur, a key district in Southern Punjab which places it closer to its target market. A wide range of financial services is offered by the bank including micro-lending, micro-insurance, Islamic banking products and deposits to the financially excluded individuals living in both urban and rural areas of Pakistan.

Ownership

Ownership Structure The Bank is a subsidiary of National Rural Support Program (NRSP) with a shareholding of ~52%. Other shareholders include International Finance Corporation (IFC), Acumen and Kreditanstalt für Wiederaufbau (KfW) – a German based Company, each having ~16% shareholding in the bank.

Stability Continued sponsor support accompanied by stable ownership pattern since inception bodes well for the bank.

Business Acumen NRSP – a nonprofit organization – established in 1991, is an autonomous body limited by government guarantee. NRSP is the largest Rural Support Program in the country in terms of outreach, staff and development activities. Other sponsors including KfW-owned by the Government of Germany, IFC-a member of the World Bank Group and Acumen-incorporated in 2001, share the common purpose to develop under privileged societies of developing economies and encourage financial inclusion.

Financial Strength Government backing to NRSP along with strong financial position of other sponsors strengthens the financial muscle of the bank.

Governance

Board Structure The overall control of the bank vests in eight members board of directors (BOD) including the CEO. The Chairman of the Board is Mr. Rashid Bajwa and Mr. Zahoor Hussain Khan is the CEO/President of the bank. Two independent directors reside the board.

Members' Profile The directors are experienced professionals having exposure in different sectors, including microfinance industry.

Board Effectiveness The Board of directors is branched into three sub-committees namely (i) Audit (ii) Remuneration & Compensation and Operational Risk and Policy. These committees ensure effective oversight of the bank's affairs and strengthens the board's governance role.

Financial Transparency M/S A.F. Ferguson & Co. are the External Auditors of the bank.

Management

Organizational Structure The bank has divided its organization structure in ten departments with each department head reporting directly to the CEO and the head of internal audit reports to the Audit Committee.

Management Team Mr. Zahoor Hussain Khan – the President and CEO – carries over ~22 years of experience in banking and finance and has been associated with the group for long. The CEO is assisted by experienced management team.

Effectiveness To ensure effectiveness of the operations, the bank has four management committees in place namely i) Operation & Risk, ii) Asset Liability (ALCO), iii) IT Steering and iv) Management Committee.

MIS Detailed MIS reports are generated to support the senior management in timely and effective decision making. MIS includes reports pertaining to disbursements, repayments, recoveries, deposits, and compliance.

Risk Management Framework The Bank has instituted policies for assessing credit worthiness of loan applicants, which is paramount to its business model. Recently, the bank has particularly steered its focus towards consolidating its position through adapting to more stringent and efficient risk control mechanism.

Technology Infrastructure The bank uses Oracle Flexcube as its core banking software; implemented since 2012. Back to back support contract from Oracle is directly in place to ensure smooth system run.

Business Risk

Industry Dynamics Pakistan Microfinance Industry comprises 44 microfinance providers including 11 Microfinance Banks (MFBs), 17 Microfinance Institutions (MFIs), 7 Rural Support Program (RSPs) and 9 others projects, MFBs dominate the Industry with a share in lending portfolio of ~68%.

Relative Position The bank catered ~15% borrowers of MFB market at End-June18, grabbing a ~10% share of the market in terms of Gross Loan Portfolio (GLP) which stood at PKR~23,917mln as at End-June-18 (End-Dec17: PKR~20,934mln) with a growth of ~14%. The bank has a market share of ~12% on the deposits side.

Revenue During the period under review, the bank's total operating income increased to PKR~2,273mln with growth of ~40% on YoY basis (1HCY17: PKR 1,627 mln). The gain is attributed by increase in Net Interest/ Markup Revenue (NIMR) which showed a growth of ~57% on YOY basis, on the backdrop of revised rates.

Profitability During the period under review, the bank's earning assets remained relatively stable at ~84% of total asset as at End-June-18. Overall profitability of the bank clocked in at PKR ~291mln increased by ~14% YoY supported by improved spread.

Sustainability The bank plans to continue strengthening its customer base by introducing new microfinance products, expanding its Islamic micro-lending division, and increasing its geographical outreach. The bank is also undergoing developments to initiate digital banking platform.

Financial Risk

Credit Risk The Bank's loan book is primarily concentrated in non-collateralized loans while advances continued to be dominated by Agri Input Loan (End-June18: ~73%), followed by Livestock Loan (End-June18: ~15%). During the period under review, the bank's NPLs ratio hiked to ~4.1% (End-Dec'17: ~0.03%). The increase is backed on account of non-payments by some sugarcane farmers. Curtailment of NPLs is essential to the profitability of the bank.

Market Risk Short term investments witnessed a major drop by ~50% in the period under review. This majorly included diminished investment in mutual funds.

Funding The bank's funding is majorly fueled through deposits, which primarily consisted of time deposits (~75%). Out of the total deposit base of the bank amounting to PKR~24.3bln, Islamic banking deposits constituted ~8%. The bank's advances to deposits ratio (ADR) stood at ~96%, representing restricted funding. Since the bank's asset base remained under pressure, it kept the deposit base stagnant to reduce/avoid any pressure exerted on spread.

Liquidity Liquidity profile decreased during the period under review as the bank's liquid assets-to-deposits and borrowings ratio dropped to ~23% at End-June18 (End-Dec17: ~34%). Reduction in lending to financial institution led to a decrease in liquid assets on overall basis.

Capital Adequacy The bank's privately placed term finance certificate redeemed on 30-June-18. Capital adequacy ratio (CAR) of the bank stood at ~17.6% as at End-June'18 (End-Dec'17: ~18.4%). The bank plans on securing a subordinated loan in CY19 to keep its CAR intact. Cautious management approach is necessitated.



NRSP Microfinance Bank Limited

	30-Jun-18	31-Dec-17	31-Dec-16	31-Dec-15
	6M	Annual	Annual	Annual
PKR mln				
BALANCE SHEET				
Earning Assets				
Finances	23,251	21,100	13,280	9,142
Investments	1,198	2,551	6,109	2,132
Deposits with Banks	4,079	5,192	4,062	1,565
	28,527	28,843	23,451	12,839
Non Earning Assets				
Non-Earning Cash	1,063	1,674	1,205	660
Net Non-Performing Finances	262	(159)	(96)	(72)
Fixed Assets & Others	4,292	3,231	1,893	879
	5,617	4,746	3,001	1,467
TOTAL ASSETS	34,144	33,590	26,452	14,306
Funding				
Deposits	24,308	23,671	16,922	7,257
Branch Banking	24,308	23,671	16,922	7,257
Branchless Banking	-	-	-	-
Borrowings	3,765	4,053	5,416	4,202
	28,072	27,725	22,338	11,459
Non Interest Bearing Liabilities	1,786	1,850	911	303
TOTAL LIABILITIES	29,859	29,575	23,248	11,761
EQUITY (including revaluation surplus)	4,283	4,012	3,203	2,534
Deferred Grants	2	2	1	10
Total Liabilities & Equity	34,144	33,590	26,452	14,306
INCOME STATEMENT				
Interest / Mark up Earned	2,989	4,976	3,221	2,054
Interest / Mark up Expensed	(1,065)	(2,039)	(1,240)	(741)
Net Interest / Markup revenue	1,924	2,937	1,981	1,313
Branchless Banking Income (excluding admin expenses)	-	-	-	-
Other Operating Income	349	871	693	601
Total Revenue	2,273	3,808	2,675	1,914
Other Income	-	-	-	-
Non-Interest / Non-Mark up Expensed	(1,363)	(2,315)	(1,559)	(1,122)
Pre-provision operating profit	909	1,493	1,116	793
Provisions	(501)	(388)	(155)	(142)
Pre-tax profit	408	1,106	960	650
Taxes	(117)	(284)	(276)	(191)
Net Income	291	821	685	460
Ratio Analysis				
Performance				
ROE	14%	23%	24%	20%
Cost-to-Total Net Revenue	60%	61%	58%	59%
Provision Expense / Pre Provision Profit	55%	26%	14%	18%
Capital Adequacy				
Equity/Total Assets	13%	12%	12%	18%
Capital Adequacy Ratio as per SBP	18%	18%	19%	21%
Loan Loss Coverage				
Non-Performing Advances /Gross Advances	4%	0%	0%	0%
Loan Loss Provisions / Non-Performing Advances	72%	331%	300%	594%
Funding & Liquidity				
Liquid Assets / Deposits and Borrowings	23%	34%	51%	38%
Advances / Deposits	96%	88%	78%	124%
CASA deposits / Total Customer Deposits	25%	38%	44%	62%
Intermediation Efficiency				
Asset Yield	21%	19%	18%	17%
Cost of Funds	8%	8%	7%	7%
Spread	13%	11%	10%	10%
Outreach				
Branches	121	104	98	67

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		Short Term Ratings	
AAA	Highest credit quality. Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments	A1+	The highest capacity for timely repayment.
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.	A1	A strong capacity for timely repayment.
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.	A2	A satisfactory capacity for timely repayment. This may be susceptible to adverse changes in business, economic, or financial 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.	A3	An adequate capacity for timely repayment. Such capacity is susceptible to adverse changes in business, economic, or financial conditions.
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	The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions.
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.	C	An inadequate capacity to ensure timely repayment.
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.		



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 surveil the opinion due to lack of requisite information.

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

Disclaimer: PACRA's ratings are an assessment of the credit standing of entities/issue in Pakistan. They do not take into account the potential transfer / convertibility risk that may exist for foreign currency creditors. PACRA's opinion is not a recommendation to purchase, sell or hold a security, in as much as it does not comment on the security's market price or suitability for a particular investor.

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.
- (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)

Proprietary Information

(23) All information contained herein is considered proprietary by PACRA. Hence, none of the information in this document can be copied or, otherwise reproduced, stored or disseminated in whole or in part in any form or by any means whatsoever by any person without PACRA’s prior written consent