



The Pakistan Credit Rating Agency Limited

Rating Report

PAIR Investment Company 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
14-Jun-2019	AA	A1+	Stable	Maintain	-
26-Dec-2018	AA	A1+	Stable	Maintain	-
13-Jun-2018	AA	A1+	Stable	Maintain	-
18-Dec-2017	AA	A1+	Stable	Maintain	-
19-Jun-2017	AA	A1+	Stable	Maintain	-

Rating Rationale and Key Rating Drivers

Development Financial institutions (DFIs) largely operate on turf common to commercial banks. Limited depth in participation towards development of long gestation projects, low funding base, and high competition become their key challenges. Joint Venture Financial Institutions are DFIs jointly conceived by the two sovereigns with primary objective of identifying and nurturing multiple development initiatives. Their ratings are mainly characterized by sovereign ownership, adequate standards of governance, and relatively conservative risk appetite.

The ratings assigned takes into account PAIR's ability to sustain its position among peers. The Company's lending portfolio enhanced, during the year, in volumes. The lending portfolio quality is deteriorated by addition of a major group into 'non-performing category'; though related provisioning has been created. This is one major reason which reduced the profitability. Management has created an adequate mix of sectors in advances, though client concentration remains high. The capital and treasury division's primary focus of investment was Government securities; minor portion vested in Equities, Sukuk & TFCs and funds. During the year, investment book remained largely same providing good cushion to liquidity. Borrowing from financial institution remains the primary source of funding, while management's attention is required for enhancing the deposit base as it lately decreased further. Liquidity position and capitalization indicators remained stable. Going forward, PAIR is focusing on strengthening the credit portfolio by tapping new customers. Management is cognizant of the fact that they need to find new niche for growth and development, hence new avenues like SME segment, are being explored. The CEO is not in Pakistan, though taking care of the company's affairs from abroad. The ratings are dependent on the company's ability to sustain its financial profile while managing the associated risks encompassing active recovery of infected portfolio. The concentration level in funding and advances needs to be pro-actively managed. Consistent efforts by the management to add further diversity to their portfolio and at the same time stability at CEO's position remains critical for the ratings.

Disclosure

Name of Rated Entity	PAIR Investment Company Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology Financial Institution(Jun-18),Methodology Criteria Rating Modifier(Jun-18),Methodology Correlation Between Long-Term And Short-Term Rating Scale(Jun-18)
Related Research	Sector Study DFIs(Jun-19)
Rating Analysts	Sehar Fatima sehar.fatima@pacra.com +92-42-35869504

The Pakistan Credit Rating Agency Limited
Profile

Structure PAIR Investment Company Limited (PAIR) was incorporated in January 2007 and commenced operations as a Development Finance Institution (DFI) on May 29, 2007.

Background Iran Foreign Investment Company (IFIC), incorporated in March 1998, and is entrusted with the objective of managing and expanding the Government of Iran's holdings abroad.

Operations PAIR's objectives include financing for SME and large industrial and commercial projects, capital and money market operations and other investment banking activities. The Company operates through its head office in Karachi and has an office in Lahore.

Ownership

Ownership Structure The company is a joint venture between Pakistan and Iran, having equal ownership stake. The Ministry of Finance (MoF) manages the ownership interests of the Government of Pakistan, while Iran Foreign Investment Company (IFIC) represents the Government of Iran.

Stability The ownership structure is same since inception and is likely to remain same in foreseeable future.

Business Acumen The business acumen of sponsors is considered good.

Financial Strength The financial muscle of sponsors is considered strong.

Governance

Board Structure PAIR's board comprises two directors representing Pakistan and three directors representing Iran. All the members of the board are independent except the MD/CEO of the company. The board members are nominated by MOF and IFIC with immediate and until further order.

Members' Profile All the board members carry vast experience from diversified sectors. Mr. Arif Ahmad Khan, nominated by MOF, is the Chairman of the board since May'18. He has served as Secretary – Finance division and carry vast experience of 35 years in public administration.

Board Effectiveness The board has formulated four board committees for effective monitoring namely 1) Audit Committee, 2) Risk Management Committee, 3) Human Resource Committee and 4) Board Strategic Investment Committee. During the year the board meetings were conducted every quarter.

Financial Transparency During CY18, the committee met four times. M/s KPMG Taseer Hadi & Co., Chartered Accountants, are company's external auditors, expressing an unqualified opinion in their audit report for the year ended December 31, 2018.

Management

Organizational Structure The functional areas are divided into: Operations, Human Resource, Credit Administration Department, Information Technology, Treasury, Credit and Risk Management, Compliance, Capital Market, SME/Leasing, Credit and Investment Banking Group (CIBG), Finance and Accounts and Internal Audit.

Management Team PAIR's management team comprises well qualified and experienced individuals, having an association with the company since long. Company's MD/CEO, Mr. Hamid Eftekhari, term started in May'17, as per the memorandum of understanding between the two sponsoring partners. Mr. Hamid, has an overall professional experience of 21 years, working with the Government of Iran.

Effectiveness To ensure effectiveness of the decision-making process, the management has setup eight committees: Asset and Liability Committee (ALCO), Management Committee (MANCOM), Investment Committee, IT Steering Committee, HR Committee, Central Credit Committee, Internal Control Monitoring Committee, and Market Risk Committee.

MIS The head of departments monitor the performance through real time based system generated reports. These reports could be generated at any point in time for monitoring daily, weekly, monthly or quarterly performance of the respective departments.

Risk Management Framework PAIR has implemented a risk management framework outlining the various roles and responsibilities for each risk unit. Credit, market, liquidity and operational risk policies have been implemented, in-line with the requirements of SBP, to measure, monitor and mitigate all risk factors. PAIR's Risk Management Department has four main functions, namely: Credit Risk, Market Risk, Liquidity Risk, and Operational Risk.

Business Risk

Industry Dynamics JVFI's witnessed slower growth (compared to last few years) in CY18 in terms of total assets and advances attributable to economic slowdown. Investment book majorly vested in government papers given investment's security. Industry's deposit base slimmed down and major reliance for funding remained on borrowing from money market. Going forward, to compete with other financial institutions (commercial banks primarily), the industry players need to build relatively unique products and services. Otherwise, JVFI's may get marginalized.

Relative Position PAIR's market share in terms of advances inched up to 9% (CY17: 7%). On funding front, market %share in terms of borrowings inched up to 7% (CY17: 6%).

Revenues During CY18, interest earned clocked in at PKR 907mln (CY17: PKR 1.0bln). The net markup revenue decline 37% YoY despite increase in lending portfolio on back of lower spreads on lending to corporate clients.

Performance Total net revenue dipped 32% YoY to stand at PKR 101mln (CY17: PKR 129mln) attributable to lower dividend income and loss on revaluation of investments. Admin and general expenses witnessed decline. However, cost to total net revenue increased to ~50% (CY17: 45%) attributable to lower total revenue. With the increase in provisioning expense, PAIR recorded net loss of PKR 10mln against net profit of PKR 230mln in CY17. No dividend was announced by the company for CY18.

Sustainability Going forward, PAIR is focusing on strengthening the credit processes and tapping the new customers. Management intends to grow the lending portfolio. The liaison cum branch office in Tehran to facilitate cross border investments is planned. In the first phase it would only be a liaison office. While in phase two it would be converted into a branch. State Bank of Pakistan has extended the validity of in principal approval as payment mechanism between Iran and Pakistan is yet to be clarified. Given current sanctions against Iran, the same seems a challenge in near future.

Financial Risk

Credit Risk During CY18, PAIR's total assets recorded an uptick of 5% attributable to sizable increase in gross advances while total investments witnessed slight decline. Net advances portfolio was enhanced and clocked in at PKR 6.2bln (end Dec17: PKR 4.6bln). Corporate segment continued to dominate the lending book. In CY18, company's advances concentration exposure remained in the following sectors – Textile (CY18: 17%, CY17: 22%, CY16: 13.2%), Petroleum (CY18: 11.1%, CY17: 0%) and Steel (CY18: 11%, CY17: 14%, CY16: 11%). PAIR maintains a sizeable portion of its finances in TFCs (CY18: 48%, CY17: 49%, CY16: 36% of total finance). Consequently, total finances witnessed an uptrend of 18% during the year.

Market Risk During CY18, investment in government securities comprises 84% (CY17: 86%) of the entire investment book. Further segregation reveals that PIBs are 25% (CY17: 14%) and T-Bills are 75% (CY17: 86%) of the government securities. T-Bills have a yield of 6.01% - 10.30% per annum and are maturing in Feb'19. While PIBs are maturing in June'28 and carry a yield of 6.57% - 9.35% per annum. With the inclining interest rate scenario, not only the investment book declined but also showed a shift from long term to short term investments i.e. from PIBs to T-Bills.

Liquidity And Funding The liquid assets (CY18: PKR ~7bln, CY17: PKR 7.4bln) continue to provide adequate cushion to the borrowings and deposits. However, attributable to sizable increase in borrowings liquidity to deposits and borrowings witnessed decline (CY18: 76%, CY17: 91%, CY16: 109%). Going forward, with expansion in funding base, maintaining the liquidity level remains vital. The relative inability of Joint Venture Financial Institutions (JVFI's) to raise low-cost funds, as they face competition from commercial banks is a major deterrent in their growth. PAIR's funding profile remained tilted towards borrowings (CY18: PKR 7.9bln, CY17: PKR 6.3bln). Deposit base stood at PKR 1.2bln (CY17: PKR 1.8bln). The management needs to improve its outreach to enhance the funding base.

Capitalization PAIR maintains a strong equity base. The capital base of the company, mainly comprising Tier-I capital provides comfort to absorb the impact of any adverse macroeconomic performance related shocks. Given the company's conservative risk appetite and a large portion of unutilized capital, the company's capital adequacy remained above regulatory requirement (CY18: 52%, CY17: 59%, CY16: 76%).



DFIs

The Pakistan Credit Rating Agency Limited

Financials (Summary)

PAIR Investment Company Limited

PKR mln

BALANCE SHEET	31-Dec-18	31-Dec-17	31-Dec-16
	Annual	Annual	Annual
Assets			
Earning Assets			
Advances	5,484	4,549	5,114
Debt Instruments	4,980	4,324	2,901
- Total Finances	10,463	8,873	8,015
Govt Securities	5,261	5,803	7,868
Equity Investments	1,032	931	1,086
Investments in Associates & Subsidiaries	-	-	-
- Total Investments	6,293	6,733	8,955
Others	166	1,062	433
Non Earning Assets			
Non Earning Cash	73	37	64
Deferred Tax	346	261	238
Net Non Performing Finances	727	91	298
Fixed Assets & Others	456	628	596
Total Assets	18,525	17,686	18,598
Liabilities			
Certificates of Investment	1,222	1,814	2,080
Borrowings	7,916	6,371	6,550
Interest Bearing Liabilities	9,138	8,185	8,630
Non Interest Bearing Liabilities	278	246	519
Equity			
Total Equity	9,181	9,293	9,367
Revaluation Surplus	(72)	(37)	83
TOTAL LIABILITIES & EQUITY	18,525	17,686	18,598

INCOME STATEMENT

Interest/ markup earned	907	1,045	1,244
Interest/ markup expensed	(473)	(387)	(533)
Net Interest/ markup revenue	435	658	710
Other Income	101	129	53
Total revenue	536	786	764
Non Interest/ Non Markup expensed	(267)	(351)	(318)
Pre-provision Profit	269	435	445
Provision/ (Reversal)	257	67	(416)
Taxes	(22)	(138)	(258)
Net Income	(10)	230	603

Ratio Analysis

Performance

ROE	-0.1%	2.5%	6.5%
Cost-to-Total Net Revenue	49.9%	44.7%	41.7%
Capital Gains/ Total Revenue	12.5%	8.8%	0.7%

Capital Adequacy

Equity / Total Assets	49.6%	52.5%	50.4%
Capital Adequacy ratio as per SBP	52.4%	59.3%	76.4%

Funding & Liquidity

Liquid Assets/ Deposits & Borrowings	76.0%	90.9%	108.7%
Finances/ Deposits & Borrowings	122.6%	109.7%	96.3%

Loan Loss Coverage

Loan Loss Provisions/ Impaired Lending	57.5%	90.5%	74.5%
Net Impaired Lending/Total Equity	7.9%	1.0%	3.2%

PAIR Investment Company Limited

Jun-19

www.pacra.co

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