The Pakistan Credit Rating Agency Limited

Rating Report

PAIR Investment Company Limited

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Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
25-Jun-2020	AA	A1+	Stable	Maintain	-
14-Dec-2019	AA	A1+	Stable	Maintain	-
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	-
23-Jun-2016	AA	A1+	Stable	Maintain	-
23-Jun-2015	AA	A1+	Stable	Maintain	-

Rating Rationale and Key Rating Drivers

JVFIs are largely engaged in providing credit lines on turf common to commercial banks. Limited growth in advances, over last many years, is evident of conservative risk appetite of these institutions. Key reliance on treasury function funded through borrowings from money market. Their ratings are mainly characterized by sovereign ownership and relatively conservative risk appetite. The ratings assigned takes into account PAIR's ability to sustain its position among peers. Enhanced net profitability was recorded in CY19 – a positive sign. The Company's lending portfolio remained largely same, during CY19. Asset quality is deteriorated, some additions in 'non-performing category, related provisioning, if any, will have implications on profitability in the upcoming year. This along with realised loss on sale of securities affected the profitability. The management is positive about healthy income from treasury function to support profitability in CY20. 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; remaining portion was vested in Equities and Sukuk & TFCs. During the year, investment book increased providing good cushion to liquidity. The company has taken sizable exposure into government securities, wherein market risk dominates. Borrowing from financial institution remains the primary source whereas COI's minuscule part of funding base. Liquidity position and capitalization indicators remained stable. Going forward, PAIR is focusing on strengthening the existing relationships. 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. However, nothing material is on the horizon, over the medium term. New MD/CEO has joined since March 1, 2020. Covid-19 has posed challenges to almost all segments of the economy, worldwide and domestically, where sectors are getting negatively impacted. The ramifications would continue to unfold, warranting vigilance and timely actions where needed.

The ratings are dependent on the company's ability to sustain its financial profile while managing the concentration level in funding and advances. Consistent efforts by the management to add new sectors/names to further diversify their portfolio, manage provisioning expense and effect on profitability and stability at MD/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	PACRA_Methodology_FI(Jun-19),Methodology | Correlation Between Long-Term And Short-Term Rating Scale(Jun-19),Criteria | Rating Modifier(Jun-19)
Related Research	Sector Study | DFIs(Jun-20)
Rating Analysts	Usama Zubair | usama.zubair@pacra.com | +92-42-35869504

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 PAIR Investment Company Limited (PICL) is a Joint Venture Investment Company which has been formed as a result of an agreement between the Governments of Pakistan and Iran. It is classified as a "Development Finance Institution" (DFI) under the regulatory control of the State Bank of Pakistan.

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

Ownership

Ownership Structure PAIR Investment Company Limited (PAIR), an equally owned joint venture between Pakistan and Iran. 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 Ministry of Finance (MoF) and Foreign Investment Company (IFIC) is considered good.

Financial Strength The financial muscle of sponsors is considered strong.

Governance

Board Structure PAIR's board comprises three directors representing Pakistan and three directors representing Iran. Last chairman of the BOD, Mr. Arif Ahmed Khan being a nominee of MOF separated from the board in March 2019 after he retired from MOF while Mr. Hemmat Jafari was replaced by IFIC in August 2019. Under the terms of the Memorandum of Understanding MD/CEO Mr. Hamid Eftekhari was appointed in August 2017. However, shortafter his appointment he was refused business visa by relevant Pakistan authorities. The matter lingered on for long, to resolve the same, his replacement Mr. Abbass Danishvar was nominated by IFIC. He has taken charge of the office of MD/CEO effective March 01, 2020.

Members' Profile All the board members carry vast experience from diversified sectors. Mr. Zahoor Ahmed, nominated by MOF, is the acting Chairman of the board since March'19. Members representing MOF has long association with different organizations in government roles.

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.

Financial Transparency During CY19, 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, 2019.

Management

Organizational Structure The functional areas are divided into: Human Resource, Credit Administration Department, Information Technology, Treasury Department and Capital Market Department, Credit and Risk Management, Compliance, Corporate 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. Abbass Danishvar, he has taken charge of the office of MD/CEO effective March 01, 2020.

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.

MIS The head of departments monitor the performance through system generated reports. These reports can be generated daily, weekly, monthly or quarterly basis to evaluate the 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, in CY19, marginal growth advances (CY19: 4%, CY18: 6%) attributable to limited market outreach as well as conservative risk appetite of the institutions. Investment book majorly vested in government papers given investment's security has witnessed significant growth. Hence, major reliance is on non-core operations for generation of income. 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, JVFIs may get marginalized.

Relative Position The Company's market share in terms of advances inched down to 7% (CY18: 9%). Significant growth (30%) recorded in investment book where major reliance is in government papers.

Revenues During CY19, interest earned clocked in at PKR 1.97bln (CY18: PKR 907mln). The net markup revenue significantly increased in CY19. (CY19: PKR 943mln; CY18: PKR 435mln) attributable to peaked out interest rates as advances recorded attrition. During 1QCY20, interest earned stood at PKR 570mln. Net markup in 1QFY20 stood at PKR 253mln. PAIR recorded net profit of PKR 83mln during 1QCY20.

Performance During CY19, total revenue increased by 69% YoY to stand at PKR 907mln (CY18: PKR 536mln) attributable to higher dividend income and mark up earned. Admin and general expenses increased 25% YoY. However, cost to total net revenue decreased to ~37% (CY18: 49.9%) attributable to higher total net revenue. PAIR recorded net profit of PKR 241mln against net loss of PKR 10mln in CY18.

Sustainability Going forward, PAIR will be following cautious lending approach while relying on investment incomes. 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.

Financial Risk

Credit Risk During CY19, PAIR's total assets recorded an uptick of 16% attributable to sizable increase in investments. Gross advances constitute ~31% of the total assets as at end-Dec19 (end-Dec18: 39%). During CY19, net advances portfolio was dipped and clocked in at PKR 10.07bln (end-Dec18: PKR 10.46bln). In CY19, company's advances concentration exposure remained in the following three segments, Corporate: 94%, SMEs: 3.8% and Individuals: 1.7%. PAIR maintains a sizeable portion of its finances in TFCs (CY19: 52%, CY18: 48%, CY17: 49% of total finance). Total finances witnessed a downtrend of ~4% during the year.

Market Risk During CY19, investment in government securities comprises 90% (CY18: 84%) of the entire investment book. Further segregation reveals that PIBs are 29% (CY18: 25%) and T-Bills are 61% (CY18: 75%) of the government securities. Currently, investment in government securities to equity base stands at ~90% whilst Investment policy of DFIs allows investment in government securities up to 200% of equity base. While the basis for building leveraged investment book may be debated, it is noteworthy that the investment policy is silent on duration that measures the extent of market risk to be assumed.

Liquidity And Funding The liquid assets (CY19: PKR ~10bln, CY18: PKR 7bln) continue to provide adequate cushion to the borrowings and deposits. However, attributable to sizable increase in investments, liquidity to deposits and borrowings increased (CY19: 87%, CY18: 76%, CY17: 91%). Going forward, with expansion in funding base, maintaining the liquidity level remains vital. During CY19, PAIR's funding profile remained tilted towards borrowings (CY19: PKR 10.9bln, CY17: PKR 7.9bln). Deposit base witnessed attrition PKR 775mln (CY18: PKR 1.2bln). The management needs to improve its outreach to enhance the funding base.

Capitalization PAIR maintains a strong equity base (1QCY19: 9.35bln, CY19: 9.41bln, CY18: 9.18bln) 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 (1QCY20: 49.9%, CY19: 58%, CY18: 52%, CY17: 59%).

PACRA

PAIR Investment Company Limited

BALANCE SHEET	31-Mar-20	31-Dec-19	31-Dec-18	31-Dec-17
	3M	Annual	Annual	Annual
Assets				
Earning Assets				
Advances	5,737	4,826	5,484	4,549
Debt Instruments	5,334	5,248	4,980	4,324
- Total Finances	**11,071**	**10,074**	**10,463**	**8,873**
Govt Securities	6,777	8,489	5,261	5,803
Equity Investments	666	960	1,032	931
Investments in Associates & Subsidiaries	-	-	-	-
- Total Investments	**7,443**	**9,449**	**6,293**	**6,733**
Others	19	234	166	1,062
Non Earning Assets				
Non Earning Cash	38	46	73	37
Deferred Tax	409	376	346	261
Net Non Performing Finances	845	531	727	91
Fixed Assets & Others	714	765	456	628
Total Assets	**20,539**	**21,475**	**18,525**	**17,686**
Liabilities				
Certificates of Investment	854	775	1,222	1,814
Borrowings	9,693	10,885	7,916	6,371
Interest Bearing Liabilities	**10,547**	**11,661**	**9,138**	**8,185**
Non Interest Bearing Liabilities	**685**	**343**	**278**	**246**
Equity				
Total Equity	9,348	9,414	9,181	9,293
Revaluation Surplus	(41)	56	(72)	(37)
TOTAL LIABILITIES & EQUITY	**20,539**	**21,475**	**18,525**	**17,686**

INCOME STATEMENT				
Interest/ markup earned	570	1,967	907	1,045
Interest/ markup expensed	(317)	(1,024)	(473)	(387)
Net Interest/ markup revenue	**253**	**943**	**435**	**658**
Other Income	16	(36)	101	129
Total revenue	**269**	**907**	**536**	**786**
Non Interest/ Non Markup expensed	(94)	(335)	(267)	(351)
Pre-provision Profit	175	572	269	435
Provision/ (Reversal)	66	177	257	67
Taxes	(26)	(153)	(22)	(138)
Net Income	**83**	**241**	**(10)**	**230**

Ratio Analysis				
Performance				
ROE	0.9%	2.6%	-0.1%	2.5%
Cost-to-Total Net Revenue	35.0%	37.0%	49.9%	44.7%
Capital Gains/ Total Revenue	0.6%	-11.2%	12.5%	8.8%
Capital Adequacy				
Equity / Total Assets	45.5%	43.8%	49.6%	52.5%
Capital Adequacy ratio as per SBP	49.9%	58.0%	52.4%	59.3%
Funding & Liquidity				
Liquid Assets/ Deposits & Borrowings	79.5%	87.1%	76.0%	90.9%
Finances/ Deposits & Borrowings	113.3%	91.2%	122.6%	109.7%
Loan Loss Coverage				
Loan Loss Provisions/ Impaired Lending	60.7%	70.9%	57.5%	90.5%
Net Impaired Lending/Total Equity	9.0%	5.6%	7.9%	1.0%

Rating Scale | Corporate

2019

Credit Rating Scale & Definitions

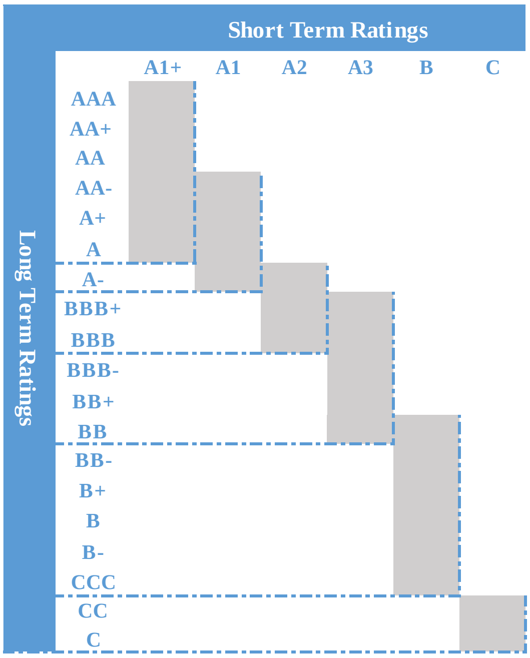
Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

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.

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

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.
(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