VIS

Credit Rating Company Limited

FUND STABILITY

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SCOPE OF CRITERIA

Fund Stability Ratings (FSRs) measure the sensitivity of a fund's Net Asset Value (NAV) and total return to changing market conditions, with particular emphasis on downside risk.

FSRs are assigned to fixed income funds, including money market and bond/Sukuk funds and Investment Plans as approved by SECP and are mentioned under the common terminology of “Fund(s)” in this FSR Methodology. These ratings incorporate an assessment of investment strategy and policies of a fund, in order to develop maximum risk estimates. These estimates are adjusted for actual investment allocations, wherever these exceed policy limits.

Funds claiming to follow a particular investment policy may drift in their investment styles. To evaluate the fund's risk profile, VIS also examines changes in the fund's investment style and approved investment policy over time. It is also pertinent to mention here that alignment of fund's risk profile with the criterion for just one of the various sources of risks for a given rating may not enable a fund to achieve the desired rating in the absence of actual asset allocation being in line with all risk related parameters. Given the minimum risk regulatory guidelines and our rating criteria, money market funds are expected to achieve higher ratings than income funds.

Pre-IPO FSR assessment of a fund is primarily based on target investment policy of the fund, in addition to our assessment of asset management expertise. Once the fund is launched, rating assessment may need to be revised for actual asset allocation in addition to the investment policy. In case, asset allocation is more aggressive in relation to investment policy, ratings may be adjusted accordingly.

Fund stability ratings, however, do not cover certain risks, emphasizing their focus on credit quality and NAV stability. These ratings do not assess management quality or operational risks, such as errors in fund administration. Broader market risks, including NAV volatility and interest rate changes, are also excluded, although weighted average maturity is considered as a factor. Regulatory risks and issuer/counterparty risks beyond credit ratings are not addressed, nor are risks tied to specific fund features or investment strategies. Additionally, extreme market conditions and tail risks fall outside the rating’s scope.

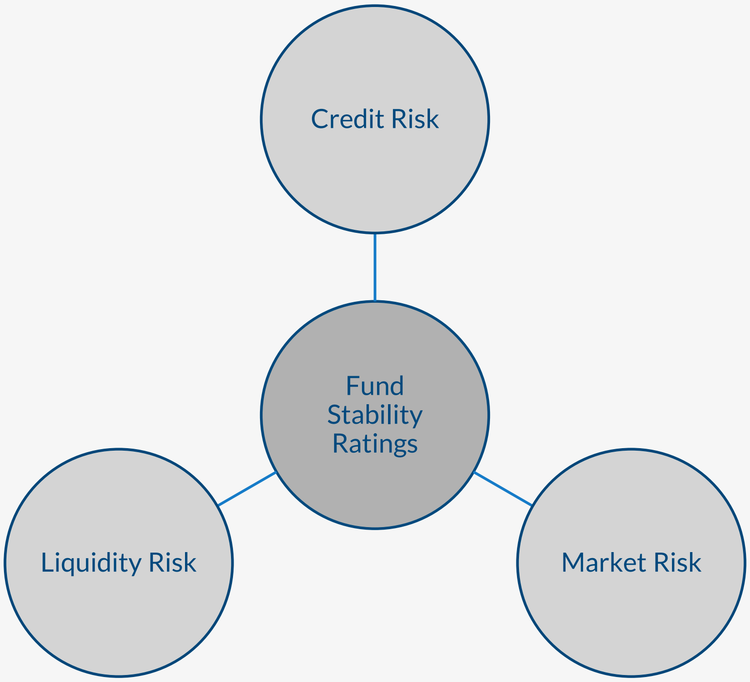
SUMMARY OF CRITERIA CHANGES

This document incorporates updates to the scope and purview of the methodology, including the coverage of investment plan.

RATING METHODOLGY

VIS fund stability ratings incorporate an assessment of various factors, including exposure to credit, market and liquidity risk. For most type of funds credit risk would carry the significant weight among rating attributes. Other rating attributes like the market risk and the liquidity risk would carry the remaining risk weight in accordance with the nature of the fund. For example, ratings of Exchange Traded Funds (ETFs) will primarily reflect the credit quality of the assets held by the fund.

Credit risk focuses on asset quality, sectoral concentrations, and adherence to investment policies, with unrated assets assigned shadow ratings. Market risk considers interest rate sensitivity, maturity, and price volatility, using metrics like modified duration. Liquidity risk emphasizes the availability of liquid assets to meet redemption demands, investor concentration, and portfolio maturity. However, the methodolgy does not cover broader market and liquidity risks due to market conditions.



Environmental, Social, and Governance (ESG) factors play a growing role in assessing fund stability, as they provide insight into non-financial risks and long-term resilience. Incorporating ESG criteria (VIS methodology link) in fund ratings evaluates the sustainability and ethical impact of investments, aligning with global trends and investor preferences.

CREDIT RISK

Assessment of credit risk incorporates exposure to credit risk both by way of asset allocation policy, actual asset allocation, credit risk due to sectoral and counterparty concentration and proportion of non-performing/restructured exposures. Fundamental to the rating analysis is a detailed evaluation of the risk profile of the assets in the fund's investment portfolio. The asset selection criteria for a fund are reviewed in context of its investment policy and objective. The evaluation of credit risk appetite of a fund requires an analysis of the investment policy in terms of proposed credit risk profile including relevant maturity and percentage holdings of these instruments. Credit quality of the portfolio is determined through an analysis of credit ratings of assets and their proportion in the fund. Where assets are not rated by VIS, shadow ratings may be assigned for evaluation of risk profile. Table 1 provides a broad outline of the expected asset quality indicator of funds with ratings in higher bands.

By way of example and to further elaborate on Table 1, for a fund stability score in the highest band, at least 85% of net assets of the fund have to be invested in 'AAA' rated exposures and investment in 'AA+' rated exposures is expected to be up to 15% of net assets. The idea is to ensure that exposures of a fund are concentrated in instruments having risk profile that is in line with the rating of the fund. If changes in a fund's risk profile over time result in assets with significantly higher or lower risk profile than indicated above, ratings may be adjusted, depending on the proportion of such assets.

Proportion of high risk assets i.e. exposures in default or under distressed restructuring, is also assessed in relation to fund size. The extent to which the return from performing assets can absorb current / future losses that may arise from high risk assets in case of missed payments or default is evaluated. In a high interest rate scenario, the cushion available for absorbing losses arising from capital erosion may be greater, subject to the fact that performing instruments in the fund are either short-term or re-price able.

VIS also reviews the fund's investments to evaluate the extent of diversification. Funds can be diversified at several levels to diminish risks associated with a certain category. VIS examines mitigation of risk through investments in different industries and different security issues within an industry, a common practice by mutual funds. Risk profile of funds is determined based on the level of diversification in the economy. However, since risk cannot be entirely eliminated through diversification, the goal should be to minimize unsystematic risk.

A. MARKET RISK

Asset Allocation % of NAV												
Asset Allocation Policy Band Limits	Issue/Issuer Rating											
	Score	AAA	AA+	AA	AA-	A+	A	A-	BBB+	BBB	BBB-	BB+
Band 1	100-90	=>85%	<=15%									
Band 2	89-80	=>50%		<=25%								
Band 3	79-70	=>25%			<=25%							
Band 4	69-60					<=15%						
Band 5	59-50						<=25%					
Band 6	49-40							<=25%				
Band 7	39-30								<=15%			
Band 8	29-20									<=25%		
Band 9	19-10										<=25%	<=10%

Overall fund risk is determined through market risk assessment in conjunction with credit risk analysis. Price fluctuations of fixed-income instruments can stem from a number of factors including interest rate movements, maturity, liquidity, credit risk and shifts in the supply & demand for each type of security. These factors combined can impact the NAV of a fund and increase its volatility. Also, price risk on TFCs remains a source of concern for income funds at large, given the lack of depth in the local debt market.

Quantitative measures such as weighted average maturity/ modified duration provide an important framework for evaluation of a fund's sensitivity to interest rate movements. A portfolio with lower sensitivity to changes in the interest rate has a more favorable impact on the fund's rating. Room for exposure to market risk in terms of maximum modified duration allowed as per investment policy that the fund can assume is an important rating criteria and carries separate weightage in the overall market risk score. Table 2 below outlines risk evaluation in terms of portfolio modified duration.

B. CREDIT RISK CRITERIA

Fund Rating	Wtd. Avg. Modified Duration
Band 1	Upto 45 Days
Band 2	46-60 Days
Band 3	61-90 Days
Band 4	91-180 Days
Band 5	181-270 Days
Band 6	271-365 Days
Band 7	366-545 days
Band 8	546-730 days
Band 9	731-1095 day

An analysis of trend of the fund's performance, its historical yield and NAV variability combined with the present investment portfolio, level of market risk exposure and market risk appetite as an indication of future composition of the investment portfolio provides a reasonable measure of NAV stability. Although an analysis of historical NAV variation does not necessarily allow us to estimate future NAV declines with high certainty, a study of empirical results nevertheless provides a good foundation for the assessment of the fund.

C. LIQUIDITY RISK

Assessment of liquidity risk profile incorporates investment in liquid avenues as a proportion of total assets in the fund being evaluated dovetailing with the investor concentration in the fund. Liquidity is of prime importance for open-end mutual funds, and is consequently assessed in detail. Inorder to meet redemption requests, funds need to maintain a certain level of liquid assets. Liquidity issues arise due to insufficient cash reserves, investments with longer maturities and a low proportion of readily marketable securities in a period of large cash outflows. Redemptions can force an open-end fund to raise cash by selling less liquid investments at depressed rates.

VIS evaluates the liquidity profile of the assets in a fund based on the market determined liquidity of such assets. For example a treasury bill carries much higher liquidity than an unlisted TFC/SUKUK and is accordingly treated. Average maturity profile of instruments held by a fund is also analyzed; the longer this measure, the higher the liquidity risk that may be associated with a fund. Liquidity assessment is also conducted in context of the fund's unit holding pattern. The mix of unit holders in terms of institutional and individual unit holders also reflect upon the redemption profile of a fund and accordingly its liquidity needs.

Concentration in unit holding pattern can potentially lead to large redemptions for open-end funds in a short interval, which can pose significant risk to a fund's ability to maintain a stable NAV. Liquidity indicators are sensitized to measure the ability of a fund to service redemptions in a timely manner.

For startup funds this data may not be available and rating ceilings may have to be applied unless specific liquidity related minimums are set by the fund for itself, to be followed till such time unit holder mix matures.

RATING SCALE & DEFINITIONS

Rating scale and Definitions may be accessed at (https://docs.vis.com.pk/docs/VISRatingScales.pdf)

Faheem Ahmad

President & CEO, VIS Credit Rating Company Limited
Founder, VIS Group Chairman,
Vice-Chairman, Association of Credit Rating Agencies in Asia

Mr. Ahmad possesses 30+ years experience in financial risk assessment with focus on Islamic finance, venture capital and general management. He has top level management experience at international level in the fields of credit ratings, Islamic and conventional financial risk assessment modeling, industrial management and construction engineering. Mr. Ahmad is an active participant at international forums on Credit Ratings. He obtained his B.S in Civil Engineering from NED University of Engineering and Technology, Karachi. He also has Masters Degrees in Engineering and Business Administration from USA.

Javed A. Callea - Member

Advisor

Mr. Callea is a professional in the financial sector with over 35 years of experience mostly in the financial institutions with certain exposure to service and infrastructure sectors in Pakistan. He has held the position of Chief Executive of a leasing company for 10 years. His core areas of expertise cover leasing, development financing, project management, investment & merchant banking, strategic investment management and real estate. Major financial institutions he worked for include Pakistan Industrial Credit and Investment Corporation, State Life Insurance Corporation, Bankers Equity, Crescent Leasing Corporation and Saudi Pak Ind. & Agri. Inv. Company. He has also served as Member Finance of Water & Power Development Authority of Pakistan and as member of the Inquiry committee on stock exchange crises in 2000 commissioned by the SECP. He earned his MBA degree from the Institute of Business Administration in 1974.

Sara Ahmed

Director - Ratings

Sara Ahmed possesses 17+ years of experience in financial risk assessment and credit structuring. She has worked in Corporate Banking & Risk Management functions locally as well as internationally. Sara has been involved in the entity ratings of numerous corporate organizations as well as financial institutions besides being part of the Methodology and Criteria Development team. She holds a Master's degree in Business Administration from the Institute of Business Administration, Karachi (2001).

Jahangir Kothari Parade (Lady LLoyd Pier) Inspired by Her Excellency, The Honorable Lady Lloyd, this promenade pier and pavillion was constructed at a cost of 3 Lakhs and donated to the public of Karachi by Jahangir Kothari to whose genrosity and public spirit the gift is due. Foundation stone laid on January 5, 1920. Opened by Her Excellency, The Honorable Lady Lloyd on March 21, 1921.

Dome: A roof or vault, usually hemispherical in form. Until the 19th century, domes were constructed of masonry, of wood, or of combinations of the two, frequently reinforced with iron chains around the base to counteract the outward thrust of the structure.

Origins: The dome seems to have developed as roofing for circular mud-brick huts in ancient Mesopotamia about 6000 years ago. In the 14th century B.C. the Mycenaean Greeks built tombs roofed with steep corbeled domes in the shape of pointed beehives (tholos tombs). Otherwise, the dome was not important in ancient Greek architecture. The Romans developed the masonry dome in its purest form, culminating in a temple built by the emperor Hadrian. Set on a massive circular drum the coffered dome forms a perfect hemisphere on the interior, with a large oculus (eye) in its center to admit light.

VIS Credit Rating Company Limited is committed to the protection of investors and offers a blend of local expertise and international experience to serve the domestic financial markets. With its international reach, VIS is positioned to aim for an international mark. In this regard, the global experience of our international affiliates and partners have been invaluable towards adding depth to our ongoing research endeavors, enriching us in ways, that enable us to deliver our responsibilities to the satisfaction of all investors. The edifice of the Jahangir Kothari Parade has stood proudly through the years and is a symbol of our heritage. Its 'Dome' as the most stable of building structures, exemplifies architectural perfection. Committed to excellence, VIS continues its endeavour to remain an emblem of trust.

INTERNATIONAL

Affiliates

Islamic International Rating Agency – **Bahrain –** iira.com
Credit Rating Information & Services Ltd. – **Bangladesh –** crislbd.com

Collaborations

Japan Credit Rating Agency, Ltd. - **Japan**
China Chengxin International Credit Rating Company Limited - **China**

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