RATING REPORT

House Building Finance Company Limited (HBFCL)

REPORT DATE:
June 12, 2020

RATING ANALYSTS:
Muniba Abdullah, CFA
muniba.khan@vis.com.pk

RATING DETAILS

	Latest Rating		Previous Rating	
Rating Category	**Long-term**	**Short-term**	**Long-term**	**Short-term**
Entity	A	A-1	A	A-1
Rating Outlook	Stable		Positive	
Rating Date	*June 12, '20*		*May 13, '19*	

COMPANY INFORMATION

Incorporated in 2006	**External auditors:** Deloitte Yousuf Adil Chartered Accountants
Unlisted Public Limited Company	**Chairman of the Board**: Mansur-Ur-Rehman Khan
Key Shareholders (with stake 5% or more):	**Managing Director**: Syed Basit Aly
State Bank of Pakistan – 90.3%	
Government of Pakistan – 9.7%	

APPLICABLE METHODOLOGY(IES)

Rating Criteria: Government Supported Entities (June 2016)
http://vis.com.pk/kc-meth.aspx

House Building Finance Company Limited (HBFCL)

OVERVIEW OF THE INSTITUTION

HBFCL was incorporated in 2006 as an unlisted public limited company with a mandate to provide financing for housing purposes.

Profile of Chairman

Mr. Mansur-Ur-Rehman Khan is a central banker having served the State Bank of Pakistan in various capacities for over 41 years. He left Deputy Governorship of SBP in 2009 on his appointment as Banking Mohtasib; a post he held for three years. Mr. Khan holds a Master's degree in Mathematics, a degree in Law and Professional qualification of DAIBP. Previously, he has served on the boards of HBFCL, Small Business Finance Corporation and Pak Kuwait Investment Company.

Profile of Managing Director

Syed Basit Aly has over 20 years of work experience. He joined civil service of Pakistan as an Assistant Commissioner in 1995. He held various field assignments in Baluchistan and later served in Ministry of Finance, GOP before joining the State Bank of Pakistan in 2003. He was director Infrastructure, Housing & SME Finance Department of State Bank of Pakistan prior to joining House Building Finance Company Limited. He holds a Bachelor's degree in Electrical Engineering from UET Lahore and a Master's degree in Development Economics from Williams College, Massachusetts, USA.

RATING RATIONALE

House Building Finance Company Limited (HBFCL) provides financing for construction, renovation and purchase of residential properties especially to the lower income strata. The company operates through 50 branches spread throughout Pakistan. It operates through a network of 51 branches, 7 area offices and 3 regional offices across the country.

Key Rating Drivers:

Ratings draw comfort from the sponsor profile of the company; stability was witnessed at the senior management level.

Sovereign ownership of HBFCL reflects strong sponsor profile of the company. HBFCL is owned by the Government of Pakistan (GoP) directly and through State Bank of Pakistan (SBP). During the years, financial assistance by the sponsor has been demonstrated to HBFCL. Profile of senior management team also remained stable with no vacancies present. Turnover was only witnessed at position of Head of Treasury, which was subsequently filled, during 2019. A new position of Deputy Managing Director was also formed during 2019. Staff strength of the company increased from 499 employees at end-CY18 to 543 employees at end-CY19. Given the recent coronavirus pandemic, the management has decided to keep its hiring plans on hold. In order to improve productivity, HBFCL implemented a performance management system along with conducting training programs and recovery incentive programs. Going forward, stability of management, along with consistency and continuity of human resource policies is considered important for future business viability and effective corporate governance.

Loan portfolio of the company remains at similar levels on account of sizeable recoveries and disbursements during the same period. Credit risk from investments is considered manageable.

Gross portfolio of HBFCL has exhibited an increasing trend and amounted to Rs. 15.2b (2018: Rs. 14.8b) at end-FY19. Growth in portfolio was achieved on the back of higher disbursements in its new products. During 2019, the company had launched two new products by the name of Ghar Pakistan Scheme and Ghar Pakistan Scheme Plus. These are construction related products; HBFCL has one more legacy construction product in its portfolio. Ghar Asaan Flexi Scheme remains the flagship product of the company with a total loan size of Rs. 9.4b at end-December 2019. While the company had made sizeable disbursements of Rs. 2.8b, it also received sizeable recoveries which translated into a stagnant net portfolio of Rs. 11.7b as of December 30, 2019. Management expects new product launches and recent organizational restructuring to aid achieving business growth targets. Disbursement targets of Rs. 4.0b for 2020 remains challenging given that the company has kept all disbursements on hold until the economic situation stabilizes. Gross portfolio of HBFCL remains stable at Rs. 15b at end-March 2020.

Asset quality indicators of the company depicted an improvement over the year. Provisioning coverage of the company also increased.

Asset quality indicators have depicted improvement with gross and net infection ratios reported at 27.8% (2018: 31.8%) and 7.4% (2018: 14.9%), respectively. With a largely stagnant financing portfolio, reduction in infection is attributed to lower quantum of non-performing loans (NPLs). As at end-2019, total NPLs were reported lower at Rs. 4.2b vis-à-vis Rs. 4.7b in the preceding year. Total recoveries amounted to Rs. 2.4b in 2019. During 2018, the company had re-strategized its business plan and decided to provide bulk financing to institutions for its employees instead of relying only on walk-in customers. As per management, while recoveries may be challenging in the ongoing year, HBFCL plans to involve the institutions for easy recovery from employees. The company also plans to roll over due principal payments by 12 months in line with the regulator's guidelines. Provisioning coverage of the company also increased from 62.4% in 2018 to 78.4% in 2019.

Profitability levels improved on account of higher return on its investment and advances portfolio; efficiency levels were reported on the higher side.

Revenue sources of the company primarily include its loan and investment portfolio while some markup income is also earned on its lending to financial institutions and bank balances. During 2019, return on investments improved significantly to Rs. 1.0b (2018: Rs. 0.5b) on account of higher benchmark rates. Investment portfolio of HBFCL largely comprises long term government paper followed by PIBs. The company also expensed financing cost of Rs. 137.5m primarily on account of utilization of funding line from Pakistan Mortgage Refinance Company; to date, HBFCL has fully utilized this fund amounting Rs. 3b. Moreover, the company also took fresh provisioning of Rs. 368.6m against its NPLs. With higher returns, bottom line profitability improved from Rs. 1.0b in 2018 to Rs. 2.8b in 2019. Nevertheless, efficiency ratio weakened on account of higher growth in expenses to 54.2% (2018: 45.9%) in 2019; with a higher headcount of employees, compensation expense increased. Future direction of earnings will be a function of quantum of disbursements and credit quality of the same, recovery from non-performing portfolio and level of administrative expenses.

Capitalization indicators have remained robust while liquidity is expected to further strengthen on the back of additional funding line.

Paid-up capital of the company remained unchanged at Rs. 19.4b, at end-December 2019. Accounting for reserves and retained profits, equity level of HBFCL was reported higher at Rs. 20.1b (FY18: Rs. 16.9b), at end-2019. Over the years, equity of the company increased primarily on the back of internal capital generation. At end-December 2019, the bank has an accumulated loss of Rs. 1.0b. With Capital Adequacy Ratio (CAR) reported at 133.4% (2018: 143.5%), bank remains at comfortable levels, above the minimum regulatory requirement depicting significant room for growth. With lower NPLs outstanding, net NPLs to Tier 1 Equity improved to 4.3% (2018: 10.4%) at end-December 2019. Liquidity avenues of the company include significant exposure in T-bills and PIBs. Liquid assets as a proportion of total liabilities remained comfortable at 208.7%.

House Building Finance Company Limited (HBFCL) Appendix I

FINANCIAL SUMMARY				*(amounts in PKR millions)*
BALANCE SHEET	**31-Dec-16**	**31-Dec-17**	**31-Dec-18**	**31-Dec-19**
Total Investments	6,841.0	6,489.5	4,010.4	10,283.8
Net Advances	11,816.9	11,512.3	11,681.1	11,668.7
Total Assets	20,906.5	20,330.1	20,877.8	25,201.8
Borrowings	-	-	-	2,000.0
Total Liabilities	4,908.3	3,616.6	3,972.6	5,093.8
Paid up Capital	3,001.0	19,365.0	19,365.0	19,365.0
Tier 1 Equity	15,998.1	16,713.4	16,905.2	20,108.0
INCOME STATEMENT	**31-Dec-16**	**31-Dec-17**	**31-Dec-18**	**31-Dec-19**
Net Mark-up Income	1,538.8	2,281.9	2,241.4	2,850.3
Net (Provisioning) / Reversal	(862.8)	678.9	348.1	(368.6)
Non-Markup Income	281.2	177.2	147.9	130.8
Administrative Expenses	1,758.1	984.6	1,404.0	1,618.4
Profit (Loss) Before Tax	(835.9)	2,019.1	1,254.5	953.7
Profit (Loss) After Tax	(866.0)	1,625.3	1,042.2	2,762.0
RATIO ANALYSIS	**31-Dec-16**	**31-Dec-17**	**31-Dec-18**	**31-Dec-19**
Gross Infection (%)	42.3%	44.7%	31.8%	27.8%
Provisioning Coverage (%)	61.0%	51.8%	62.4%	78.4%
Net Infection (%)	23.2%	28.9%	14.9%	7.4%
Cost of borrowings (%)	9.5%	-	-	8.5%
Net NPLs to Tier-1 Capital (%)	-144.2%	22.1%	10.4%	4.3%
Capital Adequacy Ratio (C.A.R (%))	-18.9%	130.5%	143.5%	133.4%
Efficiency (%)	97.0%	40.0%	45.9%	54.2%
ROAA (%)	-4.2%	7.9%	5.0%	12.0%
ROAE (%)	-12.8%	11.0%	6.0%	14.9%
Liquid Assets to Liabilities (%)	127.4%	153.8%	218.0%	208.7%

ISSUE/ISSUER RATING SCALE & DEFINITIONS Appendix II

VIS Credit Rating Company Limited

RATING SCALE & DEFINITIONS: ISSUES / ISSUERS

Medium to Long-Term

AAA
Highest credit quality; the risk factors are negligible, being only slightly more than for risk-free Government of Pakistan's debt.

AA+, AA, AA-
High credit quality; Protection factors are strong. Risk is modest but may vary slightly from time to time because of economic conditions.

A+, A, A-
Good credit quality; Protection factors are adequate. Risk factors may vary with possible changes in the economy.

BBB+, BBB, BBB-
Adequate credit quality; Protection factors are reasonable and sufficient. Risk factors are considered variable if changes occur in the economy.

BB+, BB, BB-
Obligations deemed likely to be met. Protection factors are capable of weakening if changes occur in the economy. Overall quality may move up or down frequently within this category.

B+, B, B-
Obligations deemed less likely to be met. Protection factors are capable of fluctuating widely if changes occur in the economy. Overall quality may move up or down frequently within this category or into higher or lower rating grade.

CCC
Considerable uncertainty exists towards meeting the obligations. Protection factors are scarce and risk may be substantial.

CC
A high default risk

C
A very high default risk

D
Defaulted obligations

Short-Term

A-1+
Highest certainty of timely payment; Short-term liquidity, including internal operating factors and /or access to alternative sources of funds, is outstanding and safety is just below risk free Government of Pakistan's short-term obligations.

A-1
High certainty of timely payment; Liquidity factors are excellent and supported by good fundamental protection factors. Risk factors are minor.

A-2
Good certainty of timely payment. Liquidity factors and company fundamentals are sound. Access to capital markets is good. Risk factors are small.

A-3
Satisfactory liquidity and other protection factors qualify entities / issues as to investment grade. Risk factors are larger and subject to more variation. Nevertheless, timely payment is expected.

B
Speculative investment characteristics; Liquidity may not be sufficient to ensure timely payment of obligations.

C
Capacity for timely payment of obligations is doubtful.

Rating Watch: VIS places entities and issues on 'Rating Watch' when it deems that there are conditions present that necessitate re-evaluation of the assigned rating(s). Refer to our 'Criteria for Rating Watch' for details. www.vis.com.pk/images/criteria_watch.pdf

Rating Outlooks: The three outlooks 'Positive', 'Stable' and 'Negative' qualify the potential direction of the assigned rating(s). An outlook is not necessarily a precursor of a rating change. Refer to our 'Criteria for Rating Outlook' for details.www.vis.com.pk/images/criteria_outlook.pdf

(SO) Rating: A suffix (SO) is added to the ratings of 'structured' securities where the servicing of debt and related obligations is backed by some sort of financial assets and/or credit support from a third party to the transaction. The suffix (SO), abbreviated for 'structured obligation', denotes that the rating has been achieved on grounds of the structure backing the transaction that enhanced the credit quality of the securities and not on the basis of the credit quality of the issuing entity alone.

(blr) Rating: A suffix (blr) is added to the ratings of a particular banking facility obtained by the borrower from a financial institution. The suffix (blr), abbreviated for 'bank loan rating' denotes that the rating is based on the credit quality of the entity and security structure of the facility.

'p' Rating: A 'p' rating is assigned to entities, where the management has not requested a rating, however, agrees to provide informational support. A 'p' rating is shown with a 'p' subscript and is publicly disclosed. It is not modified by a plus (+) or a minus (-) sign which indicates relative standing within a rating category. Outlook is not assigned to these ratings. Refer to our 'Policy for Private Ratings' for details. www.vis.com.pk/images/policy_ratings.pdf

'SD' Rating: An 'SD' rating is assigned when VIS believes that the ratee has selectively defaulted on a specific issue or obligation but it will continue to meet its payment obligations on other issues or obligations in a timely manner.

REGULATORY DISCLOSURES — Appendix III

Name of Rated Entity	House Building Finance Company Limited (HBFCL)
Sector	Development Finance Institution (DFI)
Type of Relationship	Solicited
Purpose of Rating	Entity Rating
Rating History	

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
RATING TYPE: ENTITY				
12-Jun-20	A	A-1	Stable	Maintained
13-May-19	A	A-1	Positive	Maintained
14-May-18	A	A-1	Stable	Reaffirmed
23-Jun-17	A	A-1	Stable	Upgraded
28-Jun-16	A-	A-2	Negative	Downgraded
30-Jun-15	A	A-2	Positive	Maintained

Instrument Structure	N/A
Statement by the Rating Team	VIS, the analysts involved in the rating process and members of its rating committee do not have any conflict of interest relating to the credit rating(s) mentioned herein. This rating is an opinion on credit quality only and is not a recommendation to buy or sell any securities.
Probability of Default	VIS' ratings opinions express ordinal ranking of risk, from strongest to weakest, within a universe of credit risk. Ratings are not intended as guarantees of credit quality or as exact measures of the probability that a particular issuer or particular debt issue will default.
Disclaimer	Information herein was obtained from sources believed to be accurate and reliable; however, VIS does not guarantee the accuracy, adequacy or completeness of any information and is not responsible for any errors or omissions or for the results obtained from the use of such information. VIS is not an NRSRO and its ratings are not NRSRO credit ratings. Copyright 2020 VIS Credit Rating Company Limited. All rights reserved. Contents may be used by news media with credit to VIS.

Due Diligence Meetings Conducted

	Name	Designation	Meeting Date
1	Mr. Ashraf Ali Velji	Chief Financial Officer	April 28, 2020