RATING REPORT

U Microfinance Bank Limited (UMBL)

REPORT DATE:
April 29, 2019

RATING ANALYSTS:
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RATING DETAILS

	Latest Rating		Previous Rating	
Rating Category	**Long-term**	**Short-term**	**Long-term**	**Short-term**
Entity Rating	A	A-1	A	A-2
Rating Date	*Jan 11, '19*		*April 27, '18*	
Instrument	A-		A-	
Rating Outlook	*Stable*		*Stable*	

COMPANY INFORMATION

Incorporated in 2003	**External auditors: KPMG Taseer Hadi & Co. Chartered Accountants (2018)**
Unlisted Public Limited Company	**Chief Executive Officer:** Syed Kabeer Abbas Naqvi
Key Shareholder(s):	
Pakistan Telecommunication Company Limited – 100%	

APPLICABLE METHODOLOGY(IES)

VIS Entity Rating Criteria: ***Microfinance Institutions (May, 2016) & Notching the Issue (June, 2016)***
http://www.vis.com.pk/kc-meth.aspx

U Microfinance Bank Limited (UMBL)

OVERVIEW OF THE INSTITUTION

UMBL (previously, Rozgar Microfinance Bank Limited) was incorporated as an unlisted public limited company in 2003 under the Companies Ordinance, 1984.UMBL is a wholly owned subsidiary of Pakistan Telecommunication Company Limited (PTCL) and a sister concern of Pak Telecom Mobile Limited (PTML) (Brand Name – Ufone).

Profile of President & CEO

Mr. Naqvi is a seasoned professional in the microfinance sector. Previously, Mr. Naqvi has served in Telenor Microfinance Bank Limited (TMBL) with his last designation being Group Executive

Director, Chief Financial Officer & Company Secretary. His overall work experience is over 15 years.

Financial Snapshot

Net equity: 2018: Rs. 2.8b; 2017: Rs. 1.4b; 2016: Rs. 1.1b

Net profit: 2018: Rs. 547.1m; 2017: Rs. 259m; 2016: Rs. 72.4m

RATING RATIONALE

Rating Rationale: The rating action incorporates improvement in funding profile and liquidity buffer of the Bank post injection of Rs. 4b Tier 2 capital by the sponsor, Pakistan Telecommunication Company Limited (PTCL). Ratings also reflect strong sponsor profile and demonstrated support of PTCL. PTCL has been assigned an entity rating of AAA/A-1+ (Triple A/A-One Plus) and is co-owned by the Government of Pakistan and Etisalat International Pakistan (LLC) (Etisalat). Improvement in financial profile of UMBL has continued on a timeline basis and is a key rating driver. Going forward, ratings are dependent on achievement of projected growth plans while improving asset quality indicators, strengthening deposit profile and retaining buffer over regulatory capital requirement.

Credit Risk: After increasing by 91% in 2017, net advances portfolio of UMBL increased by 61% in 2018. In absolute terms, net advances portfolio stood at Rs. 17b (2017: Rs. 10.6b; 2016: Rs. 5.6b) at end-CY18. Resultantly, market share in gross advances has continued to increase over the last few years. Increase in market share is a function of improved productivity indicators (active borrowers per loan officer has increased on a timeline basis) and expansion in branch network (branch network has increased from 100 branches at end-CY17 to 141 branches by end-CY18). Over 90% of the outstanding portfolio represents bullet loans. UMBL has now diversified its portfolio to around 63 districts. However, top 10 districts represent around half of the total loan portfolio. UMBL targets to open 60-70 branches in the ongoing year which will allow the Bank to achieve further geographical diversification. Livestock/crop loan remains the forte of UMBL while secured gold loans represented around 18% of the outstanding portfolio at end-Dec'2018. Infection in the financing portfolio has increased on a timeline basis but continues to remain within manageable levels despite significant growth in financing portfolio.

Liquidity: PTCL injected Tier 2 capital of Rs. 4b during FY18. The Tier-2 capital has a tenor of seven years with five years grace period. As per management, excess funds have been placed at higher rates with other financial institutions translating into a spread for the Bank. In addition, the bank has access to sizeable short term running finance lines. Liquidity profile of the bank draws support from sizeable proportion of longer maturity deposits & borrowings in funding mix and unutilized credit lines. However, depositor concentration levels continues to be on the higher side. Net advances to deposit ratio (ADR) of UMBL stood at 83% end-CY18. Improvement in deposit profile (including depositor concentration and mix) remains a key focus area of the management. Focus of new branches being opened will also be on deposit mobilization apart from undertaking financing activities.

Capitalization: Paid-up capital increased to Rs. 2.26b (2017: Rs. 1.2b) at end-CY18 on account of equity injection of Rs. 1b by sponsor. Accounting for reserves and accumulated profits, total equity of the bank increased to Rs. 2.8b (2017: Rs. 1.4b) at end-CY18. Increase in equity base alongwith additional sub-ordinated tier 2 eligible capital resulted in higher capital adequacy ratio of 19.05% (2017: 16.16%; 2016: 17.6%) at end-CY18 despite significant growth in risk weighted assets.

Profitability: UMBL posted profit before taxation of Rs. 784.3m (2017: Rs. 407.6m; 2016: Rs. 93.7m) in 2018. Increase in profitability was a function of significant growth in financing portfolio while spreads also inched upwards. Going forward, profitability of UMBL is projected to depict strong double digit on account of aggressive growth in financing portfolio. Maintaining asset quality indicators will remain important in achieving projected profitability levels.

U Microfinance Bank Limited (UMBL) Appendix I

FINANCIAL SUMMARY						*(amounts in PKR millions)*
	2018	**2017**	**2016**	**2015**	**2014**	**2013**
Total Assets	34,792	17,631	10,592	2,271	1,832	1,381
Net Advances	17,020	10,554	5,528	913	344	41
Asset Quality						
Gross Infection (PAR-30) (%)	1.27%	0.45%	0.46%	0.46%	0.08%	0.05%
Funding & Liquidity						
Deposits	20,535	11,971	8,110	1,065.30	702.6	205.2
Net Advances to Deposit Ratio (%)	83%	88%	68%	86%	49%	20%
Cost of Deposits (%)	8.5%	9.51%	9.41%	6.02%	3.60%	1.20%
Capitalization						
Net worth	2,809	1,379	1,122	1,048	957	1,039
Net Worth % Total Assets	8.1%	7.8%	10.6%	46%	52%	75%
Profitability						
Profit/ (loss) Before Tax	784	407.6	93.7	29.3	-136.7	-102.8
Profit/ (loss) after Tax	547	259.0	72.4	8	-96.9	-45.1
Number of Branches	141	100	75	38	25	15
Total Number of active clients	287,320	187,677	118,160	22,254	8786	1220
Average Loan Size	59,951	56,740	47,197	41,313	39,437	33,919

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 — Annexure-III

Name of Rated Entity	U Microfinance Bank Limited
Sector	Microfinance Banks
Type of Relationship	Solicited
Purpose of Rating	Entity & Instrument Rating

Rating History

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
RATING TYPE: INSTRUMENT				
11-Jan-19	A-		Stable	Reaffirmed
27-April-18	A-		Stable	Final
01-Mar-17	BBB+		Stable	Preliminary
RATING TYPE: ENTITY				
11-Jan-19	A	A-1	Stable	Upgrade
27-April-18	A	A-2	Stable	Upgrade
29-Sep-17	A-	A-2	Stable	Reaffirmed
28-Apr-17	A-	A-2	Stable	Reaffirmed
28-Apr-16	A-	A-2	Stable	Reaffirmed
29-Apr-15	A-	A-2	Stable	Reaffirmed
30-Apr-14	A-	A-2	Stable	Upgrade
30- Apr-13	BBB+	A-2	Positive	Upgrade/Rating Watch Removed Maintained
23- Apr-12	BB+	A-3	Rating Watch-Positive	

Instrument Structure

Instrument	Privately Placed Term Finance Certificate
Issue amount (Rs.)	600 million
Tenor	7 years
Security Structure	Privately placed, unsecured, subordinated
Grace Period	5.5 years
Repayment	Four semi-annual installments
Interest Rate	6-month KIBOR plus 3.5%

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.
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