

## RATING REPORT

## U Microfinance Bank Limited (UMBL)

**REPORT DATE:**

Feb 03, 2022

**RATING ANALYSTS:**

Maham Qasim

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## RATING DETAILS

Rating Category	Latest Rating		Previous Rating	
	Long-term	Short-term	Long-term	Short-term
Entity Rating	A+	A-1	A	A-1
Rating Date	April 30, '21		April 30, '20	
PPTFC-1	A		A-	
Rating Outlook	Stable		Rating Watch Developing	
PPTFC-2	A-		-	
TFC-2 Rating Date	Feb 03, '22		-	

## COMPANY INFORMATION

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

## APPLICABLE METHODOLOGY(IES)

VIS Entity Rating Criteria: *Microfinance Institutions (May, 2019) & Rating The Issue (July, 2020)*<http://www.vis.com.pk/kc-meth.aspx>

**U Microfinance Bank Limited (UMBL)**

OVERVIEW OF THE INSTITUTION	RATING RATIONALE
<p>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).</p> <p><b>Profile of CEO</b></p> <p>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 &amp; Company Secretary. His overall work experience is around two decades.</p> <p><b>Financial Snapshot</b></p> <p>Total Equity: 3QFY21: Rs. 6.4b; FY20: Rs. 5.7b; FY19: Rs. 3.1b; FY18: Rs. 2.8b</p> <p>Net profit: 3QFY21: Rs.854m; FY20: 906m; FY19: Rs. 254m; FY18: Rs. 547m</p>	<p>The assigned ratings to U Microfinance Bank Limited (UMBL) incorporate its strong sponsor, Pakistan Telecommunication Company Limited (PTCL) (assigned an entity rating of AAA/A-1+ (Triple A/A-One Plus) by VIS Credit Rating Company) which is co-owned by the Government of Pakistan and Etisalat International Pakistan (LLC) (Etisalat) (rated AA- by an international credit rating company). Management control of PTCL rests with Etisalat, a state owned Telecom Corporation of UAE. The implicit support from the sponsor was witnessed with the conversion of Tier-II Subordinated Debt amounting to Rs. 800.m into common equity in April'20 coupled with conversion of Rs.1.0b into preference shares to add further depth to capitalization indicators of the bank. The ratings reflect growth in business volumes, sound liquidity profile and enhanced profitability metrics. The rating action takes into account the revised business strategy in times of unprecedented pandemic situation where increased focus was aimed at enhancing secured portfolio; almost half of UMBL’s micro-credit portfolio is gold-backed entailing lower credit risk than the largely unsecured portfolio of the peer group. The lending strategy has reflected positively on capital adequacy ratio of the bank that is reported as one of the highest amongst peers. The rating derives comfort from sizable subjective provisioning booked during the period under review to add a further cushion for absorption of loan losses, if occurring, going forward. Going forward, maintenance of asset quality and liquidity indicators while continuing cautious business expansion would remain key rating drivers. In view of continued uncertainty and severity of impact of the pandemic on the economy in general and microfinance sector in particular, the outlook on the ratings will remain vulnerable.</p> <p><b>Tier-I Instrument:</b> UMBL is in the process of issuing privately placed/listed, unsecured, subordinated, perpetual, non- cumulative and continent convertible debt instruments in the form of term finance certificates (TFC) of up to Rs. 1.0b (inclusive of a green shoe option of Rs. 250m). The issue proceeds will contribute towards the bank’s additional Tier-1 (ADT-1) and will be used to support future business growth, while remaining compliant with the CAR prescribed by the SBP under its Basel III framework. Profit will be payable semi-annually in arrears on a non-cumulative basis on the outstanding issue amount.</p> <p><b>Priority with inbuilt dividend stopper clause:</b> In terms of priority of claims, UMBL’s Tier-1 instrument will rank ahead of claims of ordinary shareholders but below the bank's senior creditors, depositors. The bank cannot make dividend payments to equity shareholders in the event of non-payment of mark-up on TFCs.</p> <p><b>Non-performance risk:</b> Non-performance risk for ADT-1 instruments is characterized by presence of point of non-viability and lock-in-clause, issuer having full discretion on coupon payments, interest servicing from only profits for the year and conversion feature in the event of pre-specified trigger events in terms of regulatory requirements. While the regulatory framework may not consider a missed coupon payment as a default; the credit rating methodology employed by VIS would treat such missed</p>

payments as an event of default. In normal course of business, VIS believes that chances of non-performance risk are remote given healthy capital buffers which will be enhanced further post issuance of ADT-1 instrument. Moreover, profitability profile is expected to remain sound. Despite existence of full coupon discretion, exercising the feature is not considered likely in normal course of business as it will hamper future fund raising ability of the bank.

**U Microfinance Bank Limited (UMBL)**
**Appendix I**

<b>FINANCIAL SUMMARY</b>					
	(Rs. In millions)				
<b><u>BALANCE SHEET</u></b>	<b>Dec 31, 2017</b>	<b>Dec 31, 2018</b>	<b>Dec 31, 2019</b>	<b>Dec 31, 2020</b>	<b>Sep 30,2021</b>
Net Investments	1,786	1,968	6,970	24,075	29,728
Net Financing	10,554	17,020	21,374	30,006	32,849
Cash Balances	3,359	12,484	4,737	5,068	3,539
Total Assets	17,631	34,792	40,090	70,713	80,473
Total Deposits	11,971	20,535	23,290	46,105	50,582
Borrowings	3,069	6,010	6,733	13,274	16,510
Paid Up Capital	1,286	2,286	2,286	3,086	4,085
Tier-1 Equity	1,379	2,809	3,060	5,673	6,527
Net Worth	1,379	2,809	3,051	5,675	6,440
<b><u>INCOME STATEMENT</u></b>	<b>Dec 31, 2017</b>	<b>Dec 31, 2018</b>	<b>Dec 31, 2019</b>	<b>Dec 31, 2020</b>	<b>Sep 30,2021</b>
Net Mark-up Income	1,493	2,690	3,424	5,792	4,889
Net Provisioning / (Reversal)	86	260	838	1,580	1,044
Non-Markup Income	458	640	939	1,263	892
Operating Expenses	1,447	2,268	3,206	4,266	3,712
Profit Before Tax	407.6	784	304	1,204	1,004
Profit after tax	259.0	547	254	906	854
<b><u>RATIO ANALYSIS</u></b>	<b>Dec 31, 2017</b>	<b>Dec 31, 2018</b>	<b>Dec 31, 2019</b>	<b>Dec 31, 2020</b>	<b>Sep 30,2021</b>
Gross Infection	0.45%	1.27%	4.10%	0.1%	3.42%
Incremental Infection	0.6%	2.3%	6.2%	-0.3%	-
Provisioning Coverage	28.1%	33.2%	39.3%	20.2%	44.3%
Net Infection	0.33%	0.85%	2.53%	0.1%	1.9%
Net NPLs to Tier-1 Capital	2.5%	5.2%	17.8%	0.5%	10.1%
Capital Adequacy Ratio	16.6%	20.5%	16.7%	21.7%	18.6%
Cost of Deposits	9.5%	9.2%	11.6%	10.8%	-
Markup Spreads	20.0%	17.6%	20.5%	24.3%	-
ROAA	2.31%	2.09%	0.68%	1.6%	1.5%
ROAE	29.6%	26.1%	8.6%	20.7%	18.8%
Liquid Assets to Total Deposit & Borrowings (%)	34.0%	54.4%	39.0%	50%	51.8%

**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](http://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](http://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](http://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
<b>Name of Rated Entity</b>	U Microfinance Bank Limited				
<b>Sector</b>	Microfinance Banks				
<b>Type of Relationship</b>	Solicited				
<b>Purpose of Rating</b>	Entity & Instrument Rating				
<b>Rating History</b>	<b>Rating Date</b>	<b>Medium to Long Term</b>	<b>Short Term</b>	<b>Rating Outlook</b>	<b>Rating Action</b>
<b><u>RATING TYPE: INSTRUMENT TFC-2</u></b>					
	03-Feb-22		A-	Stable	Preliminary
<b><u>RATING TYPE: INSTRUMENT TFC-1</u></b>					
	29-April-21		A	Stable	Upgrade
	30-April-20		A-	Rating Watch Developing	Maintained
	11-Jan-19		A-	Stable	Reaffirmed
	27-April-18		A-	Stable	Final
	01-Mar-17		BBB+	Stable	Preliminary
<b><u>RATING TYPE: ENTITY</u></b>					
	29-April-21	A+	A-1	Stable	Upgrade
	30-April-20	A	A-1	Rating Watch Developing	Maintained
	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	
<b>Instrument Structure</b>	<b>Instrument</b>	<b>Privately Placed Term Finance Certificate (PPTFC-1)</b>			
	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%			
	<b>Instrument</b>	<b>Privately Placed Term Finance Certificate (PPTFC-2)</b>			
	Issue amount (Rs.)	1000 million			
	Tenor	Perpetual			
	Security Structure	The instrument is unsecured			
	Interest Rate	6-month KIBOR plus 3.5%			
<b>Statement by the Rating Team</b>	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.				

<b>Probability of Default</b>	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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Due Diligence Meetings Conducted		Name	Designation	Date
	1	Mr. Naveed Sadiq	Financial Controller	Nov 26, 2021