RATING REPORT

FINCA Microfinance Bank Limited (FINCA MFB)

REPORT DATE:
April 24, 2018

RATING ANALYSTS:

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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		Stable	
Rating Date	*April 23, '18*		*Oct 31, '17*	

COMPANY INFORMATION

Incorporated in 2008	**External auditors:** M/s Deloitte Yousuf Adil Saleem & Co
Public Limited Company	**Chairperson of the Board**: Ms. Zar Wardak
	CEO: Mr. M. Mudassar Aqil
Key Shareholders (with stake 5% or more):	
FINCA Microfinance Coopertief U.A - 86.4%	
Kashf Holdings(Private) Limited – 5.2%	

APPLICABLE METHODOLOGY(IES)

JCR-VIS Entity Rating Criteria: Micro-Finance Banks (May 2016)
http://www.jcrvis.com.pk/kc-meth.aspx

FINCA Microfinance Bank (FINCA MFB)

OVERVIEW OF THE INSTITUTION

FINCA Microfinance Bank Limited (FINCA MFB) previously Kashf Microfinance Bank Limited, was incorporated in June, 2008 as a public limited company under the Companies Ordinance, 1984. The ultimate holding company of FINCA MFB is FINCA International Inc., a not-for-profit corporation incorporated in Washington D.C., U.S.A.

Profile of Chairman

Ms. Zar Wardak serves as regional director of FINCA International (Middle East & South Asia). She carries over 10 years of experience in executive financial management.

Profile of CEO

Mr. Mudassar Aqil joined FINCA MFB as CEO in 2011. Prior to joining FINCA, he worked for 14 years at a leading commercial bank in Pakistan and the United States. He also serves as a director on the Board of Pakistan Microfinance Network.

Financial Snapshot

Net equity: FY17 – Rs. 3.3b, FY16 – Rs. 2.4b

Net profit: FY17 – Rs. 854.8m; FY16: Rs. 630.9m

RATING RATIONALE

The assigned ratings of FINCA Microfinance Bank (FINCA MFB) incorporate association of the bank with FINCA International Inc., a global microfinance organization operating in 20 subsidiaries, including Pakistan. FINCA MFB continues to receive support from its parent through transfer of technical expertise emanating from FINCA's global experience. The ratings also take into account sizeable loan book, adequate asset quality and improved profitability of the bank. FINCA MFB has embarked upon various IT initiatives which are expected to bring operational efficiencies, going forward.

Credit Risk: During FY17, loan book of the bank grew by 48% and amounted to Rs. 15.1b (FY16: Rs. 10.2b) against the target of Rs. 13.5b. Individual lending continues to remain forte of the bank, while average loan ticket size has also increased on a timeline basis. The bank's loan book reflects an adequate diversification of agricultural, livestock and enterprise loans and among Equal Monthly Installment (EMI) and Bullet repayment structures. During FY17, asset quality indicators deteriorated as gross infection increased to 1.5% (FY16: 1.1%) and incremental infection amounted to 2.9% (FY16: 1.0%). As a result, the management has embarked upon various risk mitigation initiatives including post-disbursement screening mechanism, deployment of regional compliance officers, 90-day write-off structure etc.; impact of the same will be seen over time.

Liquidity & Funding: Deposits continue to be the primary source of funding for the bank that increased to Rs. 19.2b (FY16: Rs. 11.1b) by end-FY17. Deposit mix largely remained the same with term deposits comprising more than two-third of the deposit base. During FY17, liquidity profile of the bank improved owing to decline in concentration in deposit base and higher liquid assets carried on the balance sheet. However, developing further granularity in deposit base is required to mitigate the impact of large withdrawals; till the time such granularity is achieved, the bank may need to maintain a larger liquidity cushion on the balance sheet.

Capitalization: Tier-1 equity of the bank augmented to Rs. 3.3b (FY16: Rs. 2.4b) on account of profit retention, however as a result of expansion in the microcredit portfolio along with lower proportion of gold backed loans, Capital Adequacy Ratio (CAR) decreased to 18.6% (FY16: 20.6%) by end-FY17. The bank is exploring various options to strengthen its CAR while expanding micro-credit portfolio.

Profitability: With decrease in return on mark-up bearing assets and marginal increase in cost of funds, spread of the bank declined to 20.5% (FY16: 24.0%) during FY17. However, sizeable growth in microcredit portfolio led to higher net mark-up income. Despite lower operational self-sufficiency, the bank reported a higher profit after tax of Rs. 854.8m (FY16: Rs. 630.9m) during FY17.

Information Technology: FINCA MFB is focusing towards leveraging technology for improving efficiencies and has embarked upon various IT initiatives including digital financial services project, upgradation of IT infrastructure, acquisition of new core banking software and business intelligence solution during the period under review.

FINCA Microfinance Bank (FINCA MFB) Appendix I

FINANCIAL SUMMARY			(amounts in Rs. Millions)
BALANCE SHEET	**Dec 31, 2015**	**Dec 31, 2016**	**Dec 31, 2017**
Net Investments	1,039.2	1,885.3	5,209.1
Net Financing	5,418.7	10,082.3	14,863.3
Cash Balances	766.6	2,058.2	2,533.1
Total Assets	8,451.9	15,618.0	25,141.9
Total Deposits	6,057.4	11,070.0	19,183.9
Borrowings	115.0	1,350.0	1,669.0
Tier-1 Equity	1,915.2	2,420.0	3,275.1
Net Worth	1,933.5	2,432.6	3,283.2
INCOME STATEMENT	**Dec 31, 2015**	**Dec 31, 2016**	**Dec 31, 2017**
Net Mark-up Income	1,365.1	2,338.5	3,552.5
Net Provisioning / (Reversal)	105.7	219.2	406.6
Non-Markup Income	326.2	549.8	693.5
Operating Expenses	1,340.0	1,681.4	2,461.2
Profit after tax	166.7	630.9	854.8
RATIO ANALYSIS	**Dec 31, 2015**	**Dec 31, 2016**	**Dec 31, 2017**
Gross Infection	2.3%	1.1%	1.5%
Incremental Infection	3.0%	1.0%	2.9%
Provisioning Coverage	11.4%	26.0%	35.7%
Net Infection	2.1%	0.8%	1.0%
Net NPLs to Tier-1 Capital	5.8%	3.5%	4.4%
Capital Adequacy Ratio	30.5%	20.6%	18.5%
Cost of Funds	9.2%	7.6%	7.7%
Markup Spreads	22.0%	24.5%	20.2%
OSS	111.8%	138.5%	133.3%
ROAA	2.2%	5.6%	4.2%
ROAE	10.5%	29.7%	29.8%
Liquid Assets to Total Deposit &Borrowings (%)	29.3%	31.8%	37.1%

ISSUE/ISSUER RATING SCALE & DEFINITIONS Appendix II

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: JCR-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.jcrvis.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.jcrvis.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.

'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.jcrvis.com.pk/images/policy_ratings.pdf

'SD' Rating: An 'SD' rating is assigned when JCR-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	FINCA Microfinance Bank (FINCA MFB)				
Sector	Micro Finance Bank (MFB)				
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				
	23-Apr-18	A	A-1	Stable	Reaffirmed
	31-Oct-17	A	A-1	Stable	Reaffirmed
	27-Apr-17	A	A-1	Stable	Reaffirmed
	09-Jan-17	A	A-1	Stable	Upgrade
	26-April-16	A-	A-2	Positive	Reaffirmed
	30-April-15	A-	A-2	Positive	Maintained
	30-April-14	A-	A-2	Stable	Upgrade
	30-April-13	BBB+	A-3	Stable	Upgrade
	09-May-12	BBB-	A-3	Rating Watch - Developing	Downgrade
	29-April-11	BBB	A-3	Rating Watch - Developing	Maintained
Instrument Structure	N/A				
Statement by the Rating Team	JCR-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	JCR-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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