RATING REPORT

Pak China Investment Company Limited (PCICL)

REPORT DATE:
June 26, 2023

RATING ANALYSTS:

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RATING DETAILS

Rating Category	Latest Rating		Previous Rating	
	Long-term	**Short-term**	**Long-term**	**Short-term**
Entity	AAA	A-1+	AAA	A-1+
Rating Outlook	Stable		Stable	
Rating Date	*June 26'23*		*June 23'22*	

COMPANY INFORMATION

Incorporated in 2007	**External Auditor:** Not Applicable*
Unlisted Public Company	**Chairman of the Board**: Mr. Wang Baojun
Key Shareholders (with stake 5% or more):	**Chief Executive Officer**: Mr. Jiang Ketao
Government of Pakistan – 50%	
People's Republic of China – 50%	

**The Board is not functional*

APPLICABLE METHODOLOGY(IES)

VIS Entity Rating Criteria:
Government Supported Entities (July, 2020)
http://www.vis.com.pk/kc-meth.aspx

Rating Scale
https://docs.vis.com.pk/docs/VISRatingScales.pdf

Pak China Investment Company Limited (PCICL)

RATING RATIONALE

The assigned ratings of Pak China Investment Company Limited ('PCICL' or 'the Company') incorporate implicit support of its two sovereign sponsors, Government of Pakistan (GoP) and People's Republic of China (PRC), with equal shareholding held through Ministry of Finance (MoF) and China Development Bank (CDB), respectively. CDB has an outstanding rating of 'A+' from an international credit rating agency. In the backdrop of challenging economic conditions disbursements are being made in a highly cautious and conservative manner; the Institution has embarked upon an overall consolidation strategy with sole focus on listed, rated and blue-chip clients in the medium to long-term horizon. On the other hand, PCICL is exploring the option of debt and equity exposure in high importance sectors to help promote foreign direct investment in Pakistan. The ratings reflect timeline improvement in asset quality indicators given no new case of infection was reported along with initiation of recovery from delinquent clients. However, there is room for improvement in the corporate governance environment as the Board of the Institution is currently not complete & functional. Subsequently, GoP has recently nominated a director on the Board of PCICL, regulatory approval from SBP of FPT is awaited. In addition, the assigned ratings factor in PCICL's conservative risk appetite in terms of investment policy given no investment is to be undertaken in long-term government securities coupled with stock market exposure restricted to initial public offerings only. The aforementioned strategy has assisted the Institution in successfully avoiding mark to market losses in the increasing benchmark rates scenario prevalent. Further, the ratings are underpinned by strong capitalization, sound profitability and liquidity profile, diversified revenue steam and efforts of the senior management to implement shareholders' strategic goals and vision.

Economic Review:

The economy is currently facing several challenges, including a decrease in foreign reserves, a devaluing currency, and high inflation levels. To combat rising inflation, caused by the commodity super cycle and effects of Ukraine war, the central bank has implemented stricter monetary policies, resulting in a significant increase in the policy rate. This has led to higher funding costs for banks and impacted borrowers' debt servicing ability. As a result, banks are adjusting by increasing provisions for potential loan losses and writing off non-performing loans. The economic slowdown will likely prompt stricter lending standards with banks continuing to remain heavily invested in sovereign exposures. Counterbalancing this, rising interest rates should help banks maintain their margins, partially offsetting the decline in earnings and allowing for improved profitability. However, there is increased credit risk and market risk vulnerability, especially in the face of any potential interest rate or currency fluctuations, which could impact the capitalization levels of banks. Looking ahead, the medium to long-term outlook for the fiscal account is challenging because the government is struggling to expand its revenue base. Public debt accumulation is accelerating, crowding out private sector credit. Given banking sector balance sheets highly skewed towards Government paper, this could lead to liquidity and profitability challenges, particularly for small and medium-sized banks in the future.

Corporate Profile

Pak China Investment Company Limited ('PCICL' or 'the Company') was incorporated in Pakistan as a public limited company in 2007. PCICL operates as a Development Financial Institution (DFI) under a Joint Venture (JV) agreement between the GoP and PRC; shares of PCICL are equally held by GoP through MoF and PRC through CDB. The company has its head office in Islamabad while a representative office is located in Karachi.

OVERVIEW OF THE INSTITUTION

Pak China Investment Company Limited (PCICL) was incorporated in 2007 as an unlisted public limited company. PCICL operates as a Development Financial Institution (DFI) under a joint venture agreement between its two sponsors i.e. Government of Pakistan (GoP) and People's Republic of China (PRC). The head office of the company is located in Islamabad, while representative office is situated in Karachi.

Profile of Chairman

Mr. Wang holds degrees of Masters in Public Administration and Masters in Computer Science from China National School of Administration and Harbin Engineering University respectively. He is also a Qualified Accountant and Security Practitionerr. He has over 26 years' experience of working in Development Financial Institutions, with diversified exposure in the areas of Credit Management, Finance, Research, Information Technology and Planning. Before joining PCICL, he was Head of Australian Group as Senior Commissioner of China

Development Bank (CDB).

Profile of CEO

Mr. Jiang was appointed as Deputy Managing Director of the Company in August, 2021 and assumed the office of Managing Director on acting basis in October, 2021. Prior to joining PCICL, Mr. Jiang had 22 years' of affiliation with China Development Bank (CDB), where he served at various positions in Asset Management, Credit Management, Customer Services, Global Cooperation Management and International Finance Departments.

PCICL was established to act as a bridge for promotion of bilateral trade and investment between the two countries and with an objective of financing economically viable and technically feasible projects. The Institution has played a vital role for economic development of Pakistan through active advisory role to attract Chinese investment in Pakistan and by providing wide range of financial services in infrastructure, industrial, agriculture, services, information technology, manufacturing and real estate sectors for over the last decade. As per the JV agreement between the two countries, PCICL shall consider financing on a priority basis in projects but not limited to those in which the Chinese and Pakistani investors collaborate and projects that are conducted by Chinese enterprises in Pakistan. Total staff strength of permanent employees of the institution stood at 50 (CY21: 48) at end-CY22.

Board of Directors & Committees

During the year, there was no change in Board of Directors (BoD) wherein Mr. Wang Baojun and Mr. Jiang Ketao remained as Chairman and CEO (Acting), respectively. However, the Ministry of Finance (GoP) is yet to appoint its nominee on Board. Consequently, the quorum was not complete; hence the BoD is not functional since November 2021. As a result, no Board meeting were convened during the rating review period. In addition, external auditors could not be appointed owing to absence of BoD supervision. As per the management, MoF has nominated one director whose profile has been sent to the regulator for Fit and Proper Test (FPT). Once, the fourth member is inducted the BoD will become functional. Brief profile of current members of BoD is also attached as Annexure-1 to the report.

Table 1: Board Members

	Dec'21	Dec'22
1	Mr. Wang Baojun *Chairman*	Mr. Wang Baojun *Chairman*
2	Mr. Jiang Ketao *MD/CEO (Acting)*	Mr. Jiang Ketao *MD/CEO (Acting)*
3	Mr. Wang Li *Non-Executive Director*	Mr. Wang Li *Non-Executive Director*

The role of BOD is evaluated as per State Bank of Pakistan's (SBP) guidelines through extensive evaluation framework in place; the performance is assessed on selected parameters, undertaken through a questionnaire, relating to composition, working procedure, BOD's role, oversight and relationship with the management. Evaluation is done on annual basis. Three Board level committees of the company, namely Board Audit Committee (BAC), Board Risk Management Committee (BRMC) and Board Human Resource & Remuneration Committee (BHRC) are present. During 2022, no Board committee meetings were convened.

Management Profile

The management team at PCICL is spearheaded by the MD/CEO (Acting), Mr. Jiang Ketao. As per the organogram attached as Annexure-II, heads of nine groups report to the MD/CEO, which include Investment Banking (IBG), Corporate Banking & SME (CB & SME), Risk Management (RMG), IT Group, Finance, Treasury, CPEC Promotion Group, Legal, and Compliance & HR. Head-Internal Audit reports directly to BAC, while administratively he reports to the CEO.

Six committees are present at the management level including Asset and Liability Committee (ALCO), Credit Management Committee (CMC), Procurement and Disposal Committee (P&DC), Risk Review Committee (RRC), IT Steering Committee (ITSC), and Management Committee (MC). Meetings of ALCO are held on a monthly basis, while CMC, ITSC and RRC meet on a quarterly basis or more frequently as required. The proceedings of these meetings are recorded.

Risk Management

Scope of risk management department has remained the same, involving management of the overall risk profile of the Institution by monitoring all major risks encountered by the institution including credit, market & liquidity risk, operational risk. PCICL has developed an Operational Risk Management

(ORM) Framework. The framework includes ORM Manual & Policy; the manual defines operational structure of ORMD, roles and responsibilities of the relevant personnel. It contains guidelines to conduct ORM workshop on annual basis, operational risk identification and assessment. Meanwhile, the policy includes ORM tools like Risk Control Self-Assessment (RCSA), Key Risk Indicators (KRI), incident management and data collection and scenario analysis. It also introduces risk mitigation tools to decrease the likelihood and impact of undesirable events. Under operational risk measurement, PCICL has decided to use Basic Indicator Approach (BIA) for calculating operational risk capital charge. Under BIA, PCICL is required to hold capital for operational risk equal to a fixed percentage of 15% of average positive annual gross income over the past three years. Furthermore, operational risk reporting guidelines have also been given to use operational loss reports, residual operational risk monitoring report, KRI reports along with control issue reporting and action plan. Additionally, testing procedure, spot checking and independent validation and verification by internal audit have also been explicitly defined in the manual.

PCICL had also implemented revised lending criteria, constituting, minimum & maximum threshold and risk concentrations, with an aim to filter marginal clients and book good quality asset with preference given to externally rated clients. Exposure on a single obligor and on group has been capped at 15% (FY20: 20%) and 25% (FY21: 25%) of PCICL's equity, respectively with clear instructions that excess over limit will not be allowed over and above the facility amount approved. Maximum threshold for a single borrower has also been kept in line with the SBP criteria. Sectorial limit is capped at 20% of total exposure, with exceptions for power sector (capped at 30%) and financial sector (capped at 25%). These limits are subject to be reviewed annually based on changing industry dynamics.

Obligor risk-rating (ORR) model incorporating both qualitative and quantitative factors is used for credit risk assessment of each client. Every client is given a score on a scale of 1 to 12; score of 1 to 4 depicts investment grade, 5 to 6 – speculative grade and 7 to 12 – falls under classification grade. As per management, current portfolio is predominantly rated around the band of 2 and 3.

RMG also has a Facility Risk Rating (FRR) model in place to assess the severity of loss in case of default. Rating of '1' is only assigned in case of cash collateral. RMG also monitors sectoral, single party/group-wise, and externally rated/unrated exposures against established portfolio concentration limits approved by the board. There was no breach of regulatory or internal limits during the review period. Credit risk review reports are prepared and discussed in RRC on a quarterly basis. Moreover, finance department is responsible for reporting of Capital Adequacy Ratio (CAR) NSFR, LCR and other liquidity monitoring tools.

To monitor market risk pertaining to the investment portfolio, interest rate sensitivity of the balance sheet, based on the re-pricing of assets and liabilities is monitored on a periodic basis and presented to ALCO. In addition, stress testing is performed on a quarterly basis in line with the regulatory requirements. Further, review report incorporating portfolio mix, purchase & sale transactions, valuation and yield of portfolio is also presented to ALCO on a quarterly basis.

Internal Audit

The department consists of Head Internal Audit only, and the work comprises two main activities; pre audit and post audit. Pre audit involves the assessment of day-to-day activities and transactions. For post audit, there is an internal audit plan in place. As part of the post audit process, comprehensive audit of each department is conducted every year irrespective of the risk profile. During 2022, audit of several departments including IT, RMG, Treasury, CAD, CBSME & Compliance was conducted while audit of remaining departments is expected be finalized in the ongoing year. Special assignments are also conducted as and when required by the company's management/Board Audit Committee.

Information Technology

IT department at PCICL has setup two data centers one at head office (HO) Islamabad and the other one is at branch office, Karachi. HO's data center hosts the primary domain controller server, database disaster recovery server and oracle database server for the applications. Windows server is used as the operating system with domain/network policies configured in compliance with the security policy of PCICL. All employees of the institution are assigned separate user IDs for accessing the network; these IDs are configured using the user management options in compliance with security policy of PCICL.

Backup of databases is taken thrice a day at HO for all the databases running at PCICL; the backups are scheduled to run automatically at 08:00 am, 12:30 pm and 05:30 pm. Versions of changed and deleted files are kept for 15 days and can be restored during this period. Apart from daily backup, monthly, semi-annual and annual backups are also stored. These backups are restored periodically on test server to check the validity of the backup. The backup files are copied to disaster recovery servers at HO and branch office on periodic basis. In accordance to the regulatory requirement, backups are maintained for a period of 10 years. If required, specific backup can be further retained for undefined period. To enhance the current accessibility and availability of primary RTGS setup, a DR site for RTGS has been deployed at Islamabad office during the outgoing year which is now also fully functional.

Loan Approval Process

Loan approval process at PCICL remained unchanged during the rating review period. It comprises various steps including initial screening by CB&SME and RMG, and in-principal approval by DMD and MD. After that it is formally presented to the Credit Management Committee (CMC). CB&SME initiates the credit process by drafting a proposal after conducting an initial screening of potential corporate clients. The proposal is sent to RMG for its feedback after which it is forwarded to the DMD and MD for in-principal approval. If approved, the proposal goes back to CB&SME for due diligence after which a detailed memo is presented to RMG for qualitative and quantitative feedback. Lastly, the proposal is presented to the CMC for final decision. CMC is the final approving authority and comprises MD, DMD, CFO and Group Head IBG/CB&SME while the Group Head RMG acts as an observer. For equity and financial institution exposures Head of Treasury is also a member of CMC. Disbursement of loans is carried out by the Credit Administration Department (CAD) while CB&SME & CAD are responsible for the post-disbursement monitoring of loans.

Strategic Initiatives

As per PCICL's mandate, JV signed between CDB and Ministry of Finance focuses on promoting Chinese investments; it is aimed at creating a blend of earnings from markup income, advisory income and investment income & capital gains using a three-pronged strategy focusing on commercial, Government/Public side and Chinese Initiative. The Private Equity Policy is in place explaining criteria of making investment, targeted sectors and other pertinent aspects of private equity investments. In line with downturn in economic indicators, fee income decreased to Rs. 86.3m in FY22 as opposed to Rs. 115.3m in the preceding year. Chinese projects in the pipeline include a Chinese cement company (project financing) setting up a production unit in Pakistan. The project was expected to be initiated in FY21; however, in line with prevalent economic downturn, the project achieved COD during the outgoing year. Another Chinese transaction includes a fiber optic/telecom client projected to invest USD $2.0b in Pakistan for whom PCICL has prepared the financial model.

In terms of local projects, the order book has remained adequate during the period under review. The financial consultancy contract of steel sector client with Bank of China International as joint lead financial advisors is ongoing; the transaction structure has been approved. PCICL expects to reap Rs. 100m in fee from the aforementioned transaction. Other than that, the Institution is the lead arranger for large cement sector client for provision of working capital line. Another, chemical client is also in the pipeline for working capital syndication. As a result, the management expects the overall fee based income to increase by at least 20% during the ongoing year.

Financial Analysis

Asset & Investment Mix

PCICL's total asset base increased on a timeline basis with significant increase witnessed at end of the outgoing year; the growth in asset base was largely vested in investment book and was solely supported by borrowings primarily short-term borrowings. Asset base has remained volatile during the rating review period given the Institution practices arbitrage wherein short tenor risk free investments, financed by short-term borrowings are purchased from financial institutions to earn spread. Subsequently, the total asset base was recorded lower at end-Mar'23 in line with reduction in quantum of T-Bills; the borrowings reduced by the same proportion as of investments.

Table 2: Asset Mix

(Rs. in millions)	Dec'21	Dec'22	Mar'23
Cash & Bank Balances	2,067	93	88
Balances with Other Banks	6,546	3,313	4,079
Lending to FIs	-	99	600
Investments	12,843	73,659	29,580
Advances	15,842	16,198	16,003
Fixed Assets	195	336	323
Other Assets	478	735	1,131
Total	**37,971**	**94,434**	**51,804**

Government Securities:

PCICL has always had a conservative approach towards investment portfolio; the Institution has no investment in PIBs in line with institution's strategy of curtailing investment in longer tenure securities to avoid market and re-pricing risk exposure. Amid rising interest rate scenario, the investment philosophy had a notable upside as the Institution did not have to incur mark to mark losses as faced by peer DFIs and commercial banks. On the other hand, PCICL's exposure in short-term government securities at carrying values (T-bills) increased significantly at end-FY22; the same still represented over two-thirds of the investment mix at end-1QFY23. With sizable proportion of government securities, the credit risk emanating from the investment portfolio is considered manageable in the local context. Furthermore, given short-term nature of securities, the market risk is also negligible. Subsequently, the Institution recorded a surplus of Rs. 67.2m during the outgoing year as opposed to meager deficit of Rs. 1.0m in FY21. However, due to a single steep jump of 300bps during the start of the ongoing year, the Institution had to book a deficit of Rs. 133.4m at end-1QFY23; nevertheless, the quantum of the same in terms of total T-bill portfolio is still minimal. Further, given the entire aforementioned portfolio was categorized under available for sale, other comprehensive income booked under revaluation of investments amounted to Rs. 68.8m (FY21: Rs. 20.9m) at end-FY22. Subsequently, the aggregate surplus on investments increased to 139.7m (FY21: Rs. 68.4m) by end of the outgoing year. On the other hand, on account of other comprehensive loss booked to the tune of Rs. 224.2m, the aggregate surplus changed into a deficit of Rs. 51.3m at end-1QFY23. Currently, the overall government securities portfolio is expected to mature within 45 days. As per Institution's internal policy, the aggregate investment horizon is not supposed to exceed three months at any given point.

Non-Government Debt Securities:

Listed TFC portfolio remained unchanged during the review period; the same consists of investment grade instruments offered by a commercial bank. There is no deficit booked on the listed TFC. Unlisted TFC & Sukuk portfolio mainly comprises of high-rate instruments with larger portion consisting of securities issued by financial sector. Amongst the unlisted TFC portfolio, 92% (FY21: 92%) pertained to 'A or above' rated instruments at end-FY22, therefore the credit risk originating from the same is limited. Non-performing TFCs pertaining to legacy delinquent clients were recorded at Rs. 437.5m

(FY22: Rs. 437.5m; FY21: Rs. 448.5m) at end-1QFY23. The impaired TFC portfolio includes Rs. 108.8m received pursuant to a court settlement against overdue mark-up on the classified instruments. As per prudential regulations issued by SBP, the markup against the same remains suspended/ deferred. As a result, the provisioning required against the npl TFC was recorded lower at Rs. 328.8m (FY22: Rs. 328.8m; FY21: Rs. 339.8m) at end-1QFY23. Hence, the infected TFC portfolio remains fully provided. On the other hand, surplus on performing listed non-government debt securities was booked at Rs. 52.0m during the outgoing year as opposed to Rs. 77.8m in FY21.

Equity Investments:

PCICL's exposure in listed common equity declined on a timeline largely on account of deficit amounting to Rs. 59.8m (FY22: Rs. 57.0m; FY21: Rs. 44.6m) booked by end-1QFY23. Listed equity exposure of the Institution largely includes growth shares. In addition, the Institution also has investment in preference shares of a renowned chemical company. Overall equity market exposure of PCICL has remained limited therefore credit risk emanating from the same is considered low. As per the JV mandate, PCICL can only invest in IPO transactions and is restricted from having exposure in secondary equity market transactions therefore investment in stock market will remain insignificant going forward.

Associates:

Apart from that, PCICL also has equity exposures in Central Depository Company of Pakistan Limited (CDC), Pakistan Stock exchange Limited (PSX), and Deli JW Glassware Company Limited (Deli); these entities are categorized as associates because of common directorship. Carrying value of investment in PSX decreased on a timeline due to recognition of impairment amounting to Rs. 330.0 booked at end-FY22. Moreover, reduction in investment in Deli was on account of loss from associate amounting to Rs. 14.2m incurred during the outgoing year. Going forward, management has planned to continue with the conservative approach with investment to be maintained in short term government securities amid weak macro-economic conditions and volatility in interest rates.

Table 3: Investments at Market value

(Rs. in millions)	Dec'21	%	Dec'22	%	Mar'23	%
Federal Government Securities:						
T-Bills	4,496	35.0%	63,655	86.4%	19,785	66.9%
Shares:						
Listed Companies	238	1.9%	219	0.4%	217	0.7%
Preference shares	351	2.7%	392	0.5%	377	1.3%
Non-Government Debt Securities:						
TFCs-Listed	261	2.0%	261	0.4%	261	0.9%
TFCs & Sukuks-Unlisted	5,739	46.0%	8,160	11.0%	7,969	26.9%
Investment in Associates:						
Pakistan Stock Exchange Limited	722	5.6%	408	0.5%	410	1.39%
CDC of Pakistan Limited	368	2.9%	387	0.5%	384	1.30%
Deli JW Glassware	190	1.5%	176	0.2%	176	0.6%
Total	**12,843**	**100%**	**73,659**	**100%**	**29,580**	**100%**

Credit Risk

With additional liquidity channelized towards investment portfolio on account of general consolidation of lending book despite increase in disbursements *(including running finance facilities)* to Rs. 11.7b (FY21: 13.5b) for FY22; PCICL's Gross Loan Portfolio (GLP) only increased marginally by 3.6% to Rs. 17.5b (FY21: Rs. 16.9b) at end-FY22 as opposed to notable growth of 36.8% in the preceding year. In addition, the growth further slowed down during the ongoing year with GLP remaining intact at Rs. 17.6b at end-1QFY23. Sindh has remained the major geographical area of disbursement constituting 61% (2021: 38%) of fresh lending during the outgoing year. PCICL continues to focus on top-tier blue chip clients, rated clients pertaining to investment grade category and CPEC related projects. In addition, the entire covid related portfolio is settled and is currently regular. For the ongoing year, given weak macro-economic environment PCICL will continue to implement consolidation with the aim of keeping GLP at current levels. On the other hand, the management plans to increase non-funded exposure during FY23. New disbursements majorly were extended to Food, Soap, Steel, Power and Textile sectors during FY22. In terms of sectoral concentration, Power and Textile sectors constituted the highest share at end of the outgoing year. There was no internal breach in terms of sector limits and per party/group limits faced during the outgoing year Going forward, emphasis would remain on essential sectors including education and pharmaceuticals.

Industry Sectors	**Dec'21**		**Dec'22**	
Gross Advances	**Rs. in m**	**%**	**Rs. in m**	**%**
Textile	2,161	12.8%	3,388	19.4%
Chemical & Pharmaceutical	1,000	5.9%	945	5.4%
Cement	601	3.6%	330	1.9%
Sugar	1,049	6.2%	250	1.4%
Electronics & Electrical Appliances	969	5.7%	750	4.3%
Construction	500	3.0%	-	-
Power	2,960	17.5%	4,203	24.0%
Transport, Storage & Communication	1,730	10.2%	1,900	10.9%
Financial	267	1.6%	178	1.0%
Services	1,425	8.4%	1,425	8.1%
Mining	1,630	9.6%	700	4.0%
Basic Metals	659	3.9%	1,151	6.6%
Rubber & Plastics	190	1.1%	190	1.1%
Food	669	4.0%	774	4.4%
Soap Industry	439	2.6%	476	2.7%
Individuals	146	0.9%	150	0.9%
Others	500	3.0%	695	4.0%
Total	**16,896**	**100%**	**17,506**	**100%**

Given PCICL mainly focusing on top tier and high rated clients, the concentration in advances portfolio remained on the higher side. On basis of total funded and non-funded exposure, Top-10 exposures accounted for 55% (Dec'21: 43%) of total portfolio as at end-Dec'22 while concentration of Top-10 funded exposures to GLP was also recorded higher at 54% (Dec'21: 46%) as at Dec'22.

Asset Quality:

Asset quality indicators have improved on a timeline as depicted by decline in gross and net infection owing to a combined outcome of no new infection case reported coupled with aggregate recovery worth Rs. 103m made from two delinquent clients during the review period. The NPLs declined by the same number during the outgoing year. In addition, incremental recovery of Rs. 23m from the same client was registered resulting in further decline in quantum of NPLs at end-1QFY23. In addition, the provisioning coverage also improved during the review period as the management deliberately forgo the forced sale value (FSV) benefit available given the Institution had reaped sizable profit during the outgoing year; the same was done as a matter of prudence to add cushion in specific provisioning coverage. The Institution has carried out full provisioning for majority of its infected portfolio. There are only two clients on which the 100% provisioning has not been taken till date. Specific provisioning is not required for one energy sector client as it was classified as OAEM at the time of restructuring; post restructuring now the client is performing and regularly servicing its obligations. The second client belongs to food sector on which the provisioning of 62% has been carried out. In addition, PCICL provided general provisioning to the tune of Rs. 223.4m (FY21: Rs. 208.4m) during the outgoing year, on the anticipation that challenging economic conditions may have an adverse impact on performing loans and risk of increase in NPLs cannot be precluded. The management is also negotiating with some other clients to reach out of court settlements by entering into restructuring arrangements. Maintaining credit quality profile is considered important from the rating perspective amidst current macroeconomic environment.

	Dec'21	Dec'22	Mar'23
Non-Performing Loans (Rs. in m)	1,632	1,529	1,506
Gross Infection (excluding write-offs)	9.7%	8.7%	8.6%
Net Infection	4.9%	2.7%	2.7%
Provisioning Coverage	51.9%	70.9%	70.5%

**no history of write-off in last five years*

Funding & Liquidity

The overall liquidity profile of the Institution is strong and has improved during the rating review period as evidenced from liquid assets to total deposits and borrowings recorded at 85% (FY22: 69%; FY21: 70%) at end-1QFY23. Sizable treasury operations funded by secured borrowings continue to support the liquidity indicators. The coverages are in sync with the benchmarks for the assigned rating; the maintenance of liquidity buffers at current levels will remain important from ratings perspective going forward. Secured commercial borrowings continue to comprise the major portion of borrowing mix. Other sources of funding mix included borrowings from SBP under refinance scheme (LTFF) and Temporary Economic Relief (TERF), borrowings obtained against charge on book debts/receivables, repo borrowings and unsecured borrowings.

In contrast to peer DFIs, as at Dec'22, the maturity mismatch was only present 1-7 days bucket as the Institution does not invest in long-tenor government securities; the management monitors maturity mismatch on an ongoing basis to mitigate the associated risk. Furthermore, given PCICL as a DFI is a secondary market borrower with deposits only restricted to certificate of investments (COIs), the liquidity risk arising from withdrawals is almost non-existent. The COIs decreased to Rs. 1.5b in FY22 as opposed to Rs. 4.8b at end of the preceding year owing to maturity of the existing contracts. In line with increasing benchmark rates scenario prevalent the customers tend not to lock in their capital in COIs. Going forward, borrowings will continue to remain the key source of financing for the Institution. COIs will not be a part of funding plan in near future, and will only be considered if positive spreads are on offer.

Rs. In m	Dec'21	Dec'22	Mar'23
Liquid Assets	13,960	68,034	27,955
Liquid Assets (adj for collateral)	12,994	13,144	13,591
Borrowings & Deposits	19,444	73,681	30,383
Borrowings & Deposits (adj for. collateral)	18,478	19,109	16,036
Liquid Assets-to-Total Deposits and Borrowings	70.3%	68.8%	84.8%

Profitability

PCICL's profitability profile has exhibited positively trajectory during the outgoing year primarily owing to growth in the earning asset base as the spreads largely remained unchanged, significant uptick in non-markup income, sizable improvement in efficiency indicator and conservative investment policy leading to avoidance of mark to market losses. The spreads only increased by meager 10bps owing to varied factors including higher cost of funding originating from policy rate hikes evidenced during the outgoing year, transfer pricing delay in increase in policy rate to be passed on to the borrowers and increased contribution of investments and bank deposits income entailing lower yield to the markup income. The non-markup was recorded higher at Rs. 795.5m (FY21: 351.5m) in line with foreign exchange income to the tune of Rs. 687.3m (FY21: Rs. 251.4m) booked during FY22 owing to significant rupee depreciation experienced during the outgoing year. As per the management, almost one-fourth of PCICL's equity is still kept in Dollar denomination to reap forex gain; no conversion in Pak Rupee is expected in the foreseeable future. Subsequently, in line with the aforementioned PCICL recorded notably healthy bottom line of Rs. 1.2b (FY21: Rs. 773m) during FY22.

Interest earned on advances increased to Rs. 2.0b (FY21: Rs. 1.2b) mainly on account of higher yield on advances recorded at 12.4% (FY21: 9.0%) as there was only marginal increase in the net advances portfolio. Moreover, exponential growth of around 2.4x was evidenced in markup earned on investments; the same increased to Rs. 3.3b (FY21: 1.4b) in line with sizable growth in quantum of short-term risk-free government securities coupled with higher yield of 10.2% (FY21: 7.5%) reaped during the outgoing year. The increase in yield of advances and investment portfolios was underpinned by higher average benchmark rates recorded during FY22. As a result, overall yield on interest bearing assets increased to 10.4% (FY21: 7.2%) during FY22. On the other hand, total markup expensed also increased significantly to Rs. 3.2b (FY21: Rs. 1.2b) in line with surge in secured-borrowings to Rs. 54.2b (FY21: nil) along with SBP's policy rate being at the very high end of the spectrum at end-FY22. Resultantly, cost of borrowing and cost of funds was recorded at 9.0% (FY21: 6.0%) and 9.2% (FY21: 6.2%) respectively during the outgoing year. Subsequently, in line with higher cost of funding largely offsetting increase in yield on earning assets, the Institutions' markup spread increased slightly to 1.1% in FY22 as opposed to 1.0% in the preceding year.

PCICL's spread size continues to be low as a combined outcome of inherent limitations of business model and operational phenomenon; prior to FY22 the Institution was mainly funded by equity therefore, there was notable mismatch in yield on assets and cost of liabilities recorded. In addition, the treasury function only avails arbitrage opportunities on short term money market instruments (T-bills) funded by short term secured/repo borrowings with zero investment made in PIBs entailing higher interest yield in comparison to T-Bills. However, the aforementioned conservative take has helped the Institution with evasion of heightened market risk in the current increasing benchmark rate scenario prevalent.

	2021	2022
Average Return on mark-up bearing assets	7.2%	10.4%
Cost of Funds	6.2%	9.2%
Spread	1.0%	1.1%

Apart from growth in foreign exchange income, the non-markup income was supported by reduction in net loss on securities recorded at Rs. 19.8m in FY22 as opposed to Rs. 42.6m in the preceding year; the same is net figure of realized and unrealized gain/loss wherein the major portion is unrealized. On the other hand, fee income reduced to Rs. 108.0m (FY21: Rs. 129m) in line with reduction in investment banking fees to Rs. 35.1m in FY22 in comparison to Rs. 54.8m in the previous year. Further, in terms of growth in asset base and topline, the Institution managed to rationalize operating expenses at Rs. 610m (FY21: 534.2m) despite commodity super cycle evidenced during FY22. Subsequently, efficiency ratio improved on a timeline basis given the uptick in recurring income outpaced increase in operating expenses. The Institution's efficiency compares favorably to peers. On the other hand, PCICL recorded a notably higher provisioning charge of Rs. 572.1m (FY21: Rs. 220.3m) mainly in line with impairment loss of Rs. 330.0m booked on equity investment in an associate.

Maintenance of asset quality in the current economic downturn from putting a drag on profitability is considered important from ratings perspective. On the other hand, the management's aim to focus on agro-based lending, Fintech sector, development of short-term factoring/discounting lending products and investment banking income is expected to provide positive impetus to bottom line going forward. The successful materialization of the same will be ascertained over time.

The uptick in profitability indicators continued in the ongoing year as well with the Institution reporting sizable profit of Rs. 1.0b in 1QFY23 in comparison to Rs. 244.1m in the corresponding quarter last year. The positive momentum was supported by growth in net interest income, significant foreign exchange gain and streamlined operating expenses. On the other hand, fee income dipped in the outgoing year owing to slow-down in economy as Investment banking department was largely impacted. However, several deals of project financing, debt syndication and others are in the pipeline and expected to materialize during FY23. Therefore, management expects fee-based income to grow notably in the ongoing year. Moreover, collaborations have been undertaken with Chinese companies for investment in Pakistan particularly in the agriculture sector. Under the aforementioned arrangement, production facilities will be established in Pakistan yielding import substitution and offering an avenue for exports. For this, PCICL will provide advisory services and may even provide partial funding going forward.

(Rs. in millions)	2021	2022	1Q2023
Net Mark-up Income	1,468	2,376	864
Fee Income	129	108	13
Dividend Income	0	6	0
Foreign Exchange Income	251	687	848
(Loss)/Gain on Securities	-43	-20	-19
Share in Profit of Associates	68	42	13
Operating Expenses	534	610	161
Provisions	220	572	(23)
Efficiency	29%	19%	9%
Profit after Tax	773	1,226	1,010

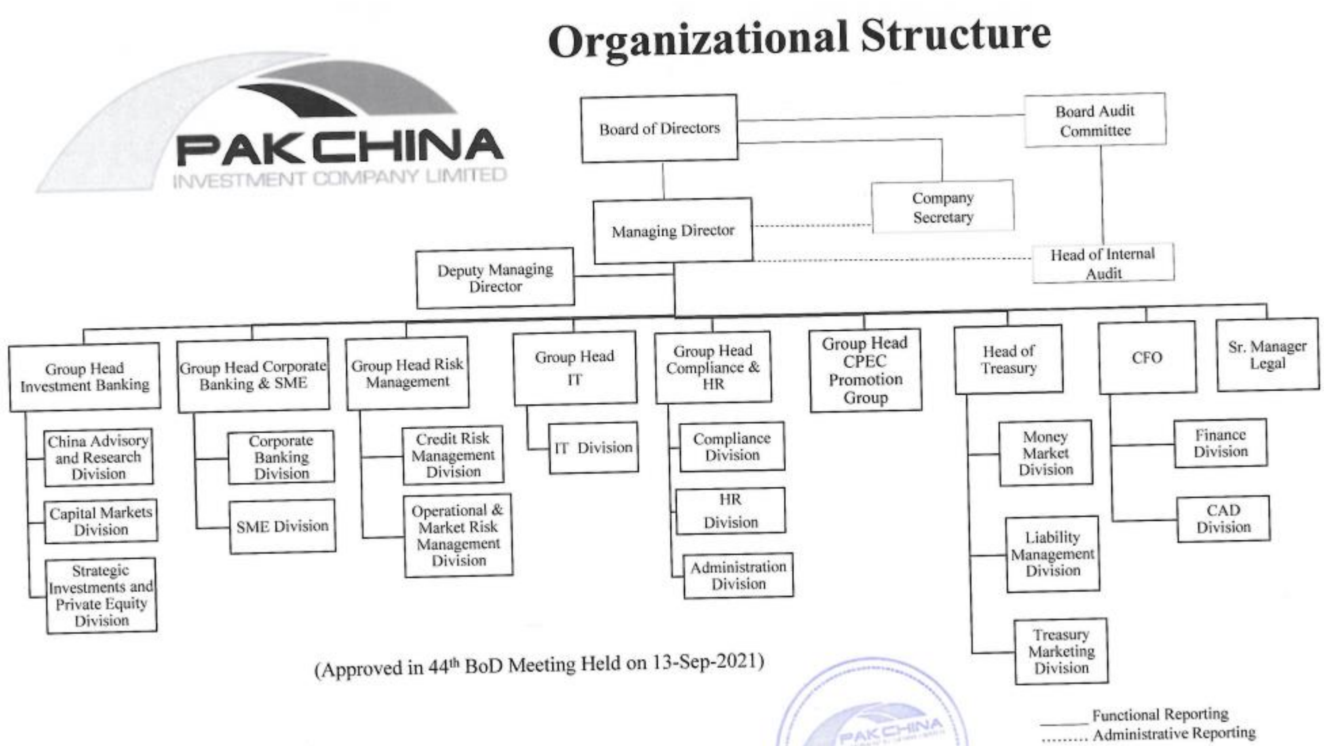
Capitalization

Paid-up capital of the Institution increased to Rs. 9.9b (FY22: Rs. 9.9b; FY21: Rs. 9.7b) by end-1QFY23 on account of transfer from advance against issue of shares head worth Rs. 209.3m in the outgoing year; equal shares were issued to both sponsors. PCICL maintains the highest initial paid-up capital amongst all DFIs. Moreover, the Tier-1 equity *(CAR statement)* and net worth (excluding revaluation on fixed assets) has augmented on a timeline basis largely in line with sizable internal profit generation. Further as a combined impact of enhancement of equity base coupled with reduction in npls, net npls to tier-1 capital decreased during the rating review period; the same is in line with the benchmark of the assigned rating. PCICL's Risk Weighted Assets (RWAs) increased by 13% Y/Y to Rs. 27.8b (FY21: Rs. 24.7b) at end-FY22 largely owing to higher RWAs recorded amid increase in market risk. Marginal increase was recorded in credit RWAs in line with higher advances portfolio recorded. Despite slight decline in Capital Adequacy Ratio (CAR) on a timeline to 57% (FY22: 54.7%; FY21: 62.8%) at end-1QFY23, CAR is strong and considerably higher than the minimum regulatory requirement of 11.5% and represents sizable room for growth for the institution. In addition, PCICL's CAR is one of the highest in the DFI sector; the same has been taken positively from the ratings perspective. The Institution has enhanced its portfolio of rated clients over time and will continue to do so; the same is expected to assist in keeping the CAR strong at current levels.

Pak China Investment Company Limited (PCICL) Annexure I

Mr. Wang Baojun *Chairman*	Mr. Wang carries more than 21 years' experience of working in Development Financial Institutions with diversified exposure in the areas of Credit Management, Finance, Research, Information Technology and Planning. Mr. Wang holds degrees of Masters in Public Administration and Masters in Computer Science from China National School of Administration and Harbin Engineering University, School of Computer & Information Science, respectively. He is also a Qualified Accountant and Security Practitioner. During his affiliation with CDB, he lately held positions of Division Director of Credit Management and Division Director of International Cooperation & Study in International Finance Department, while he also served as Deputy Division Director of Confidential Affairs and Deputy Division Director of General Affairs in General Office.
Mr. Jiang Ketao CEO/MD (Acting)	Mr. Jiang was appointed as Deputy Managing Director of the Company in August, 2021 and assumed the office of Managing Director on acting basis in October, 2021. Prior to joining PCICL, Mr. Jiang had 21 years' of affiliation with China Development Bank (CDB), where he served at various positions in Asset Management, Credit Management, Customer Services, Global Cooperation Management and International Finance Departments. He has also accomplished various international investment ventures of CDB as Senior Appraisal Specialist and Senior Negotiator. His last posting at CDB was as Director of Coordination Division, International Finance Department of CDB. Mr. Jiang received his degrees of Master's in Finance and Bachelor's in Economic Information Management from Jiangxi University of Finance & Economics, China.
Ms. Wang Li *Non-Executive Director*	Ms. Wang joined the Board of Directors of PCICL in October, 2018 as non-executive Director. She is Deputy Director General of Market Development & Equity Investment Department of China Development Bank (CDB). She joined CDB's predecessor China Investment Bank in 1987 and has held many positions in the Bank over the past three decades, including Division Chief of Corporate Bond Underwriting Division in Treasury & Financial Market Department, and Vice President of CDB Securities Co. Ltd. Ms. Wang currently serves on professional committees of numerous self-regulatory organizations.

Pak China Investment Company Limited (PCICL) **Annexure II**



Pak China Investment Company Limited (PCICL) Annexure III

FINANCIAL SUMMARY	*(amounts in PKR millions)*				
BALANCE SHEET	**Dec'19**	**Dec'20**	**Dec'21**	**Dec'22**	**Mar'22**
Total Investments	19,241	15,658	12,843	73,659	29,580
Net Advances	9,291	11,550	15,842	16,198	16,003
Lending to Financial Institutions	-	1,150	-	99	600
Cash & Balances	3,176	2,223	2,067	93	88
Other Assets	1,691	828	7,219	4,385	5,533
Total Assets	33,400	31,409	37,971	94,434	51,804
Borrowings	16,119	12,903	14,694	72,178	30,036
Deposits & other accounts	-	512	4,750	1,503	347
Other Liabilities	649	511	251	978	159
Paid-Up Capital	9,697	9,697	9,697	9,906	9,906
Tier-1 Equity	14,483	14,549	15,508	15,245	16,147
Net Worth (Exc. Surplus on Reval.)	16,632	17,399	18,171	19,603	20,361
INCOME STATEMENT	**2019**	**2020**	**2021**	**2022**	**1Q23**
Net Mark-up Income	1,713	1,439	1,468	2,376	864
Net Provisioning / (Reversal)	472	117	220	572	(23)
Non-Markup Income	263	284	352	796	846
Operating Expenses	476	492	534	610	161
Profit Before Tax	1,066	1,166	1,133	2,032	1,585
Profit After Tax	760	773	773	1,226	1,010
RATIO ANALYSIS	**2019**	**2020**	**2021**	**2022**	**1Q23**
Gross Infection (%)	9.9%	13.6%	9.7%	8.7%	8.6%
Provisioning Coverage (%)	59.7%	39.9%	51.9%	70.9%	70.5%
Net Infection (%)	4.2%	8.6%	4.9%	2.7%	2.7%
Cost of funds (%)**	7.6%	12.0%	6.2%	9.2%	NA
Markup Spreads (%)**	2.0%	-1.8%	1.0%	1.1%	NA
Net NPLs to Tier-1 Capital (%)	2.8%	6.9%	5.1%	2.9%	2.8%
Capital Adequacy Ratio (CAR) (%)	73.7%	70.7%	62.8%	54.7%	57.0%
Efficiency (%)	23.7%	29.5%	27.7%	18.9%	9.2%
ROAA (%)*	2.9%	2.4%	2.2%	1.9%	5.5%
ROAE (%)*	4.8%	4.5%	4.3%	6.5%	20.2%
Liquid Assets to Deposits & Borrowings (%) *(adjusted for collaterals)*	31.3%	54.4%	70.3%	68.8%	84.8%

**Annualized*

***Cost of funds and Markup Spreads for 2021 & 2022 has been calculated on 5-point average method*

REGULATORY DISCLOSURES	Appendix V
Name of Rated Entity	Pak China Investment Company Limited (PCICL)
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		
26-June-23	AAA	A-1+	Stable	Reaffirmed
23-June-22	AAA	A-1+	Stable	Reaffirmed
28-June-21	AAA	A-1+	Stable	Reaffirmed
25-June-20	AAA	A-1+	Stable	Reaffirmed
21-June-19	AAA	A-1+	Stable	Reaffirmed
20-June-18	AAA	A-1+	Stable	Reaffirmed
30-June-17	AAA	A-1+	Stable	Reaffirmed
28-June-16	AAA	A-1+	Stable	Reaffirmed
24-June-15	AAA	A-1+	Stable	Initial

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. For conducting this assignment, analyst did not deem necessary to contact external auditors or creditors given the unqualified nature of audited accounts and diversified creditor profile. Copyright 2023 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	Date
1	Syed Mehar Ali Shah	Financial Controller	May 23, 2023
2	Mr. Abbas Athar Hamadani	Group Head Corporate Banking	May 23, 2023
3	Mr. Tariq Mehmood	Group Head Investment Banking	May 23, 2023
4	Syed Nabeel Abbas	Head of Treasury	May 23, 2023
5	Mr. Umer Farooq	Group Head Risk Management	May 24, 2023
6	Mr. Armughan Ahmed	CFO	May 24, 2023
7	Mr. Saeed Ahmed Khan	Head Internal Audit	May 24, 2023
8	Mr. Khurram Shahzad	Group Head Compliance	May 24, 2023