RATING REPORT

Pakistan Mortgage Refinance Company Limited

REPORT DATE:
April 06, 2020

RATING ANALYSTS:
Talha Iqbal
talha.iqbal@vis.com.pk

Asfia Aziz
asfia.aziz@vis.com.pk

RATING DETAILS

Rating Category	Latest Rating		Previous Rating	
	Long-term	Short-term	Long-term	Short-term
Entity	AAA	A-1+	AAA	A-1+
Rating Date	*April 06, 2020*		*May 07, 2019*	
Rating Outlook	Stable		Stable	
Outlook Date	*April 06, 2020*		*May 07, 2019*	

COMPANY INFORMATION

Incorporated in 2015	**External auditors:** KPMG Taseer Hadi & Co Chartered Accountants
Public Unlisted Company	**Chairman of the Board:** Rehmat Ali Hasnie
Key Shareholders (with stake 5% or more):	**Chief Executive Officer/Managing Director:** Mudassir H. Khan
Private & Public Sector Institutions – 67.2%	
Government of Pakistan – 32.8%	
Aggregate Public Sector Shareholding – 49%	

APPLICABLE METHODOLOGY(IES)

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

Pakistan Mortgage Refinance Company Limited

RATING RATIONALE

Pakistan Mortgage Refinance Company Limited (PMRC) was established by State Bank of Pakistan (SBP) in 2015 as Pakistan's first national mortgage refinance institution for provision of long-term funding to both conventional and Islamic Partner Financial Institutions (PFIs). PMRC was granted Business Commencement Certificate by SBP on June 12, 2018. Shareholding structure of the company depicts that around 67.21% stake is vested with 9 Financial Institutions including private & public sector institutions while remaining interest is held by Government of Pakistan (GoP) through Ministry of Finance (MoF). Aggregate public sector shareholding is 49%.

Key Rating Drivers

Assigned ratings are underpinned by strong Government and Regulatory Support

The assigned ratings are underpinned by PMRC's special policy role in promoting and facilitating home ownership & housing finance in the country and close linkages with SBP and GoP. Strong government and regulatory support to PMRC is evident from relaxation in meeting minimum equity requirement, foreign currency risk on World Bank loan being borne by GoP, low risk charge of 10% for PMRC on exposure to PFIs and tax exemption to investors for investment in PMRC bonds, inclusion of PMRC bonds in level 2A high quality liquid assets and exemption from maintenance of general reserve against portfolio refinanced by PMRC.

Despite subdued macroeconomic environment, low mortgage finance penetration along with significant and growing deficit of housing units in the country is expected facilitate demand growth of house finance in the country

Housing gap in Pakistan is estimated at around 10 million units with the same increasing on a timeline basis by 0.7 million units every year. The combined volume of outstanding housing finance from banks and the HBFCL stood at Rs. 103b (2018: Rs. 92.4b, 2017: Rs. 82.6b) at end-Dec'19 growing at a rate of 12% over the last two years. However, Pakistan's mortgage to GDP ratio is well below than that in South Asia. Contribution of Islamic mortgage loans in the total house financing portfolio has noted a sizeable increase and was reported at 53% (2018: 44%) at end-2019. Over the long-term, VIS expects low mortgage finance penetration along with significant and growing deficit of housing units in the country to facilitate demand growth of house finance in the country.

Refinancing portfolio witnessed sizeable increase during 2019 and in the ongoing year. Credit risk on the portfolio is considered minimal given sound credit risk management strategy in place.

Refinancing portfolio amounted Rs. 7.7b (2018: Rs. 1.2b) at end-2019 constituting disbursements to six Islamic and conventional PFIs. Focus of PMRC would be on disbursing financing through Islamic mode which over the long-term will constitute majority of the refinancing portfolio. In order to facilitate borrowers in terms of certainty of loan repayments, management plans to promote fixed rate mortgages for the initial three years which are then allowed to be rolled-over at market prices up to 25 years. PMRC also envisages undertaking programme based lending for middle and low income groups. Broad parameters, eligibility criteria and pricing for the same have been developed and documented. Going forward, PMRC envisages bringing six new large banks on board with refinancing portfolio expected to clock in at around 18b at end-Dec'20.

Credit risk emanating from the refinancing portfolio is considered minimal on account of financing with recourse to PFIs and 25% overcollateralization on Mortgage Loan Portfolio (MLP). Moreover, quarterly and monthly monitoring of the loan portfolio is

OVERVIEW OF THE INSTITUTION

Pakistan Mortgage Refinance Company Limited (PMRC) operates as a Development Finance Institution under State Bank of Pakistan (SBP) regulations. Additionally, Securities & Exchange Commission of Pakistan (SECP) oversees PMRC's capital market operations.

Profile of Chairman

Mr. Hasnie has been a member of the Board of PMRC since May 2016 and the Chairman of the Board of Directors since April 2017. He is a financial markets profession with a MA Degree in Development Banking from The American University (USA) and a nominee Director on PMRC of National Bank of Pakistan (NBP), where he is presently the SEVP & Group Chief of the Inclusive Development Group (IDG). IDG is NBP's most recent and ambitious initiative to position the Bank as not only a commercial bank but also as an institution focused on the priority financing sectors of Pakistan's economy. In this regard, not only is the focus of IDG the SME and Agriculture lending but also mortgage lending (especially promotion of home ownership for low income households). Earlier, Mr. Hasnie was heading investment banking at NBP. His over 25 years of work experience includes economics research, capital markets, investment banking, treasury and credit markets at various institutions in Pakistan. He has also served on the Boards of Pakistan Mercantile Exchange Limited, Fauji Akbar Portia Marine Terminals Limited, Agritech Limited, First Credit Investment Bank Limited and First National Bank Modaraba as a nominee director of NBP.

Profile of CEO/Managing Director

Mr. Mudassir H. Khan is the MD/CEO of Pakistan Mortgage Refinance Company. Mr. Khan holds an Executive Masters in Business Administration (update) from Stern School of Business, New York, USA and a

Masters in Finance from St. John's University, New York, USA. With over 28 years of diversified banking experience primarily covering Retail, Corporate & Investment Banking, Operations, Risk and Development Banking. Before joining PMRC, Mr. Khan worked with National Bank of Pakistan for four years as SEVP/Group Chief Retail & Commercial Banking and as Group Chief Payments & Digital Banking. Prior to that, he was with HBL for nine years, holding different portfolios as SEVP Group Head Global Operations, CIO, CCO and Head of Basel and Operational Risk. He also worked with the World Bank for more than fourteen years in the area of Financial Sector and Private Sector Development, South Asia Region, based in Pakistan and also worked in Afghanistan, Bangladesh, Nepal, Maldives; as well as in the Africa Region in Ghana, Uganda, Kenya and Sierra Leone. Before joining the World Bank, he worked in the field of Corporate and Investment Banking with Citibank, N.A and Bear Stearns in Pakistan and in USA.

Mr. Khan has been the Chairman of NBP Fullerton Asset Management (NAFA) and of First Women Bank Limited (FWBL). He was also on the Board of Directors for National Institute of Financial Transactions (NIFT); ISM and FWBL and was the Chairman Audit Committee & Risk Management Committee for FWBL and member HR and Compensation Committees for NIFT."

undertaken by the operations department whereby defective loans including prepaid and non-performing loans are replaced with fresh loans.

Credit and Market risk emanating from the investment portfolio is considered on the lower side

Investments in PIBs and T-Bills was reported at Rs. 8.8b (2018: Rs. 1b) at endd-Dec'19. Credit risk emanating from the investment portfolio is low as exposure is undertaken only in sovereign instruments. Exposure to market risk has been maintained on the lower side. Sensitivity of ratings to credit and market risk while being present is considered low.

Conservative funding strategy entailing close matching of the duration and maturity of assets and liabilities. Moreover, liquidity buffer in terms of liquid assets is expected to remain satisfactory despite sizeable growth in refinancing portfolio.

PMRC has availed borrowing of Rs. 12.7b at end-Dec'19 including Rs. 7.05b as sub-ordinated loan, from World Bank (WB) via GoP at a fixed rate of 3% per annum. The loan has a 30 year term with 5 years grace on Principal repayment. The foreign exchange risk on this loan is carried by GoP. WB, GoP and PMRC are discussing an additional credit line at concessionary rates. The securing of the funding line will further strengthen liquidity position of the Company and will support future growth plans. In order to mitigate liquidity risk, stringent maturity matching of bonds and loans is undertaken. Despite sizeable growth expected in refinancing portfolio, liquidity buffer of PMRC projected to be satisfactory over the rating horizon, in terms of liquid assets available to meet unexpected shortfalls in cash flows.

Sound Capitalization Indicators

Paid-up capital and net equity stood at Rs. 3.7b and Rs. 4.7b, respectively at end-Dec'2019. As per regulatory requirement, PMRC is allowed to operate with a minimum equity requirement of Rs. 3.5b for the first 5 year of operations subject to restriction on dividend payout. As per the Agreements between the Government of Pakistan, the World Bank and PMRC, the sub-ordinated debt if needed, can be converted into non-participatory Additional Tier 1 Capital to meet the MCR. Moreover, IFC has given in principle approval for equity investment of Rs. 500m in capital of PMRC. The inflow is expected in 2020 after completion of all legal, regulatory and other terms and conditions. Given healthy projected profitability, equity base is projected to grow over the next three years on the back of profit retention. With increase in refinancing portfolio, risk weighted assets are projected to grow but only at a limited pace given the low risk weight on financing extended to PFIs. Ratings incorporate projected Capital adequacy ratio of PMRC which will remain comfortably above statutory requirement over the rating horizon.

Profitability drivers include higher volumetric growth. Efficiency of the institution is expected to remain strong despite projected increase in operating expense given projected improvement in core revenue.

Net mark-up income increased significantly to Rs. 1.2b (2018: Rs. 223.6m) owing to higher refinancing and investment portfolio during 2019. Given healthy spreads and increase in operating expenses in line with growth in operations, net profit after tax increased to Rs. 901.8m (2018: Rs. 55m) during 2019. For the year 2020, spreads are expected to remain healthy given that higher rates have been locked in on a sizeable portion of the investments. Going forward, profitability will be driven by volumetric growth in earning assets. While remaining within manageable levels, operating expenses will increase as the company scales up its operations with general & administrative expenses representing the largest proportion of cost base. Despite increasing administrative expenses, efficiency (cost to income) ratio of the institution is expected to remain strong given projected improvement in core revenue.

Pakistan Mortgage Refinance Company Limited — Appendix I

FINANCIAL SUMMARY *(amounts in PKR millions) – Annexure I*			
BALANCE SHEET	**2017**	**2018**	**2019**
Investments	-	1,010	8,822
Net Advances	-	1,200	7,729
Total Assets	1,321	3,750	19,577
Borrowings	-	-	7,566
Deposits & other accounts	-	-	-
Subordinated Loans	-	-	7,051
Paid Up Capital	150	3,659	3,659
Tier-1 Equity	148	3,702	4,607
Net Worth	150	3,713	4,696
INCOME STATEMENT			
Mark-up/return/profit/interest earned	73	224	1,529
Mark-up/return/profit/interest expensed	-	-	(337)
Net Spread Earned	73	224	1,193
Provisions and write-offs net	-	-	-
Non-Markup Income	2	0.03	0.92
Administrative expenses	(80)	(167)	(272)
Profit/ (Loss) Before Tax	(6)	57	902
Profit / (Loss) After Tax	(4)	55	902
RATIO ANALYSIS			
Capital Adequacy Ratio (CAR)	36%	542%	207%
Liquidity Coverage Ratio (LCR)	NA	141%	382601%
Net Stable Funding Ratio (NSFR)	NA	219%	307%
Leverage Ratio	11%	99%	24%
Efficiency	111%	75%	23%
Current Ratio	NA	NA	NA
Cash flow from operations	22	(2,058)	2,666
ROAA	NA	2.2%	7.7%
ROAE	NA	2.8%	21.7%
Liquid Assets to Deposits & Borrowings	NA	NA	149%

RATING SCALE & DEFINITION 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	Pakistan Mortgage Refinance Company Limited
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				
April 06, 2020	AAA	A-1+	Stable	Reaffirmed
May 07, 2019	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. VIS is not an NRSRO and its ratings are not NRSRO credit ratings. 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. Contents may be used by news media with credit to VIS.

Due Diligence Meetings Conducted

	Name	Designation	Date
1	Mr. Zulfiqar Alam	Group Head Business and Products	19-March-2020
2	Ms. Farheen Amjad	Head of Finance	19-March-2020
3	Mr. Omair Farooqi, FCA	CFO & Group Head Operations	19-March-2020