VIS

Credit Rating Company Limited.

ESG RATING METHODOLOGY

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SCOPE OF CRITERIA

The criteria 'Environmental, Social & Governance (ESG)' applies to a wide range of Industrial and services sector non-financial corporate ESG ratings conducted by VIS Credit Rating Company Limited (VIS). The ESG methodology also applies to financial institutions including commercial banks, insurance companies, DFI's etc. since their financial and lending activities trigger same kind of risks. ESG methodology identifies the risks related to Environmental, Social and Governance factors which can impact the sustainability of the entities in the long run. It also identifies the opportunities that entities can use for their benefit in order to outperform their competitors by complying with the ever growing regulatory requirements under ESG framework.

AN OVERVIEW OF RATINGS FRAMEWORK

The ESG rating methodology would provide a rank system or scoring, appraising the environment, social & governance activities & prospects of an entity or issuer in any industry. The Environmental, Social and Governance (ESG) matters have indisputably moved to the forefront as investors are increasingly incorporating sustainability factors into their investment decisions. Companies that effectively communicate their sustainability strategies improve their capital raising abilities have an overall competitive advantage. Globally, regulators are also recognizing importance of ESG reporting and disclosures to assess the impact of ESG risks and opportunities.

Sustainable Developmental Goals (SDGs) are part of United Nations (UN) 2030 agenda for sustainable development, which was adopted by all member states in 2015 including Pakistan. SDGs can help in aligning sector and company specific ESG factors with broader societal and environmental goals. The United Nation Principles for Responsible Investment (UN PRI) is the world's leading proponent of Responsible investment. It works to understand the investment implications of environmental, social and governance (ESG) factors and to support its international network of investor signatories in incorporating these factors into their investment and ownership decisions.

ESG considerations must be material to the likelihood of default, financial stress and credit loss which may impact credit rating outcome. Thus, VIS' ESG scoring may impact either positively or negatively on the final outcome of the credit ratings. The six Principles for Responsible Investment are a voluntary and aspirational set of investment principles that offer a list of possible actions for incorporating ESG issues into investment practices. These principles are: (1) Incorporate ESG issues into investment analysis and decision-making processes. (2) Incorporate ESG issues into ownership policies and practices. (3) Seek appropriate disclosure on ESG issues by the entities. (4) Promote acceptance and implementation of the Principles within the investment industry. (5) Work together to enhance effectiveness in implementing the Principles. (6) Report on activities and progress towards implementing the Principles.

RATING METHODOLOGY

ESG refers to a broad range of qualitative and quantitative factors that relate to the sustainability of an issuer and to the broader impact on society of its businesses, investments and activities. Examples include a company's carbon footprint or the accountability of a company's management on the actions taken by them. In ESG grading, the main focus is on the aspects of ESG that can have a material impact on the credit quality of an issuer. Some ESG issues may have greater downside risk than upside potential. For example, a company with a track record of health and safety violations may face litigation risks whereas another company with strong governance structure can have proper risk assessment and informed decision making which help in achieving long term credit worthiness.

Our assessment of the exposure to E, S and G risks or benefits is based on the general ESG principles described in this methodology and the scores provide a consistent way to express this assessment. VIS will typically consider the credit impact of the distinct aspects of ESG for an entity in our analysis, as well as the combined impact of ESG considerations. For example, a company could have excellent governance and employee relations that does not offset the negative credit impact of a large carbon footprint.

In order to be meaningful for ratings, ESG considerations must be material to the likelihood of default and credit loss. Issuers encounter a multitude of ESG risks and opportunities, many of which have little tangible impact on operating or financial performance. For example, a company's volunteer work, charitable activities and other such initiatives are important to the extent that they produce social value, but their potential positive impact on the company's financial health or credit standing is unlikely to be material, however, these factors may have a positive impact on its franchise value and enhance visibility with the stakeholders. The materiality of a particular aspect of ESG is typically specific to a sector or an issuer or a transaction. For example, air pollution emission standards may be an important credit issue for the auto manufacturing sector but may not be meaningful for media companies.

Our approach to ESG considerations is an assessment of the impact on an issuer's cash flows and the value of its assets overtime; the stability of cash flows and assets in relation to the issuer's debt burden and other financial obligations. For example, for a non-financial corporate, we assess how ESG issues such as product safety and carbon transition risks influence credit drivers such as demand for its products, cost of production, need for financing to make capital expenditures as well as the changes to these drivers over time. For financial institutions, we assess how ESG issues such as governance and customer relations influence credit factors such as the issuer's ability to access funding in markets, its liquidity, risk tolerance, capital position, profitability and other governance issues that can affect the sustainability of the FI's business model.

A. ENVIRONMENTAL RISK ("E")

Environmental risks are a significant consideration for a large number of issuers in the public and private sectors. Environment risk is broadly categorized into two segments:

I. The consequences of regulatory or policy initiatives that seek to reduce environmental trends or hazards.

- Regulations that have been implemented or those that are likely to be introduced (by the regulators or binding agreements under an international accord) with impact on the credit profiles of issuers and sectors.
- Longer-term regulatory initiatives where implementation is unclear or subject to delays provide less visibility into the likely impact on the relative risk of default and credit loss for issuers.

II. The adverse effects of direct environmental trends and hazards such as pollution, drought, severe natural and human-caused disasters and climate change.

Environmental considerations are often a source of risks for enterprises. Regulatory or policy initiatives aimed at reducing or preventing negative environmental hazards may affect market demand, revenue, costs or cash flow for issuers. Based on the above, we broadly classify the environmental risks that are generally most relevant from a credit perspective into five categories. These are (i) carbon transition; (ii) physical climate risks; (iii) water management; (iv) waste and pollution and (v) natural capital.

Carbon Transition	Physical Climate Risks	Water Management	Waste and Pollution	Natural Capital

Given that most of the environmental factors don't have measureable output, it is important that the entities should have related policy documents in place. If need arises, an external ratification may also be sought from independent bodies that provide specific certification to support the view. In 2020 acknowledging the importance of independent opinions on ESG, The International Capital Market Association (ICMA) issued global guidelines for Second Party Opinion (SPO) Providers, an institution with environmental/ social/ sustainability expertise that is independent from the entity being assessed. A 'Second Party Opinion' normally entails an assessment of the alignment of the issuer's Green, Social and Sustainability Bond issuance/ framework/ program with the outlined principles. In particular, an SPO can include an assessment of the entity's overarching objectives, strategy, policy, and/or processes relating to environmental and/or social sustainability.

A. (I) Carbon Transition

Tightening of global or national regulatory regimes related to carbon dioxide and other greenhouse gases may affect business models and their longterm financial & strategic planning. For some issuers, the shift to a lower carbon economy may reduce demand, increase compliance costs or necessitate significant investment to get expected return on assets. An entity's business mix, including its exposure to the hydrocarbon value chain and the contribution of different activities to revenue, profits and cash flow is typically an important consideration. The extent to which operations are subject to changes in technology, market and policy changes related to carbon transition may also indicate inherent risk exposure.

Entities that diversify their business mix from higher risk to energy efficient products and technologies offset major risk and has the potential to get competitive advantage as compared to the ones that fail to change. The entity's efforts to shift from high carbon emission to lower carbon renewable resources will diversify risk and improve revenue streams in the long run.

Financial institutions with a high concentration of exposure to counterparties or sectors involved in carbon dioxide and other greenhouse gases typically have the highest carbon transition risk. However, the financing of green technologies (e.g. renewable energy) by financial institutions may be beneficial and it would positively impact the carbon transition risk score. Financial institutions also face financial and reputational risks through a failure to adapt to changes in the business environment prompted by higher carbon transition risks. Financial institutions that support and serve environment friendly counter parties may be viewed favorably by the society.

A. (II) Physical Climate Risk

The nature and the location of an issuer's activities may be impacted by weather, land, water or events like hurricanes, floods, wildfires, etc. For example, droughts may affect production or input cost while floods and hurricanes may damage infrastructure and disrupt operations. Assets in low-lying coastal areas are more susceptible to rising sea levels and storms whereas the risk of wildfires is more prevalent near forested areas.

The severity and frequency of these events have increased in recent years causing significant economic losses, hazards for the local population and environmental damage. Relevant considerations for an enterprise with at-risk assets may include reserves or insurance to help recoup damagerelated costs. Some entities may have lower intrinsic exposure because their activities are less reliant on physical facilities and the cost of insurance or reserves buildup may not be relevant consideration due to high cost.

The demand of products or services may vary based on long-term trends and hazards. For example, customer demand may increase or decline with extended periods of higher temperature as well as climate events. Relevant considerations may be to diversify products offering.

Financial institutions are also exposed to climate risk and also affect insurers' underwriting exposures, the creditworthiness of financial institutions' counterparties and the value of invested assets. The increasing incidence of catastrophe losses linked to climate change and the buildup of physical climate risk as a result of chronic trends create additional underwriting and risk management complexity for financial institutions & insurers.

A. (III) Water Management

Freshwater scarcity can negatively impact a country's economic stability. This category focuses on the management of water resources which include water consumption, availability, pricing, quality and pollution, which may affect profitability. Environmental restrictions may affect an enterprise's ability to operate while violation of regulations related to water usage (e.g., overuse or pollution of water) may result in fines or cancellation of permits. Enterprises that rely heavily on water as a critical component of operations generally have higher exposure to water management risk and water stress (i.e. a greater supply & demand imbalance).

An issuer that needs a significant amount of water to operate may compete with local communities for limited water resources, for example, food production may receive priority in water usage over other products and services like tanneries, textiles and paper industries. Relevant considerations may include an issuer's consumption patterns, availability, ease of access and distribution, quality, pricing and water costs relative to overall costs of the product or service.

Enterprises with a track record of significant enforcement actions against them and poor governance around water management generally have higher risk than entities with better water management practices or those with limited water usage. Mismanagement of water resources may also have negative repercussions for the reputation of financial institutions perceived to have financed the entities that are involved in mismanagement.

A. (iv) Waste and Pollution

Pollution may harm the health of the local population including plants and land which may lead to clean-up costs, ongoing monitoring and regulatory compliance cost, fines, community health concerns and reputational risk. Increased consumer focus on pollution and waste may reduce demand for products.

Enterprises that are perceived to be significant contributors to waste and pollution may face both diminished demand and increased environmental restrictions. However, these trends may create market opportunities for enterprises selling products or services related to recycling and reuse of products. Enterprises that generate pollutants and hazardous waste, material clean-up concerns or require higher packaging generally have more inherent risk exposure.

Relevant considerations may include amount of pollution and waste creation, compliance with waste disposal and pollution regulations, use of recycled content and renewable sources in production, history of waste and pollution-related violations, fines and settlements. To help offset pollution, entities should have policies that explain how the issuer deals with reduction in waste and pollution, waste treatment technologies, packaging efficiency and increased recycling to ensure regulatory compliance.

Waste and pollution principally affect insurance underwriting exposures and may also impact the creditworthiness of financial institutions' counterparties. Financial institutions could also be subject to reputational risks if they are perceived to have facilitated damage to the health of a local population or to natural resources, for example by providing financing or insurance to polluting companies.

A. (v) Natural Capital

An enterprise's level of reliance on the natural resources and environment to provide goods and services generally indicates its exposure to natural capital risk. Damage to the ecosystem caused by enterprises can lead to a loss of revenue, consumer backlash, increased environmental compliance costs and regulatory penalties.

An enterprise with more reliance on air or land resources would be more affected by degradation of the environment caused by the enterprise. Extractive industries such as mining may damage the land, soil or forest through the course of operations, creating potential risks related to land reclamation and land governance. Significantly altering the natural environment could lead to penalties, lower future revenue and cleanup & restoration expenses.

Preventive measures, effective policies and corrective actions taken to ensure compliance with restrictions and regulations may help to offset credit risk. Usage of renewable energy for production, transmission, products & appliances, promotion of energy efficient buildings, appliances & products and adoption of day light savings can reduce reliance on natural capital thereby reducing risk of penalties and lawsuits. Damage or degradation of natural assets may also have negative repercussions for the reputation of financial institutions perceived to have financed the counterparties that caused damage.

B. SOCIAL RISK ("S")

VIS views social considerations as falling broadly into two categories (i) issuer-specific considerations, such as product safety problems that harm an issuer's reputation, (ii) the adverse effects of external factors, such as regulation that leads to higher compliance costs or creates rigid work rules.

In our assessment of social risk, we seek to assess how social risks such as poor labor relations, higher employees' turnover or labor unrest would affect revenue and increase cost. We may also consider the potential for costly settlements, fines and higher insurance premiums resulting from substandard health and safety practices or products and services perceived to be harmful. We may also consider how social risks could damage a company's reputation, which can lead to shifts in consumer preferences or even boycotts.

We broadly classify social risks that are generally most relevant from a credit perspective into five categories: (i) customer relations; (ii) human capital; (iii) demographic and societal trends; (iv) health and safety; and (v) responsible production.

These five categories help to frame the most material social issues that stem from an issuer's interaction with its major stakeholder groups. They tend to fall into one of two broader themes; those which are issuer-driven, such as how a company manages its health and safety practices, and those that are externally driven, such as the effect of changing demographics on demand of an enterprise's product.

Customer Relations	Human Capital	Demographic & Societal Trends	Health and Safety	Responsible Production

B. (I) Customer Relations

The issuer's customer interactions may have significant consequences for its reputation and future earnings. Reputational impact on customer relations may stem from a variety of sources, for example, data leakages, product safety, hiring practices, etc. Information security is critical aspect of customer relations.

Data breaches may result in fines, reputational damage and loss of market share. An enterprise that stores significant amounts of personal data or confidential information may have greater potential risk exposure. For these issuers, a track record for maintaining the integrity of its information technology and other storage systems to protect customer data and confidential information may be relevant considerations. Issuer's data protection procedures & policies and the composition & strength of dedicated information security staff along with their skill level may be important considerations as well.

Regulatory restrictions on price, marketing activities, tax structure & fines can constrain an issuer's engagement with its customers that may result in increased costs or reduced revenues. Regulations or pressure from regulators may also limit an enterprise's pricing flexibility, for example, pharmaceutical industry, energy sector, etc., issuers may gain a competitive advantage or face disadvantages due to their relative ability to comply with regulations. Customer retention strengthened through customer engagement and superior product or services is a relevant consideration.

Some industries face more stringent disclosure regulations because of greater potential health and safety implications for consumers. Relevant considerations may include severity of complaints as well as fines and lawsuits. Robust IT systems, strong framework for ensuring data security and compliance with relevant regulations may help entities offset potential customer relation risks. The ability to quickly adapt to changing consumer preferences may also offset risk or create competitive advantage.

Financial institutions are also exposed to customer relation risks through customers' perception of the fairness and integrity of their actions and behaviors. Examples include mis-selling, unfair customer treatment, insufficient disclosures, data security and customer privacy breaches.

Mis-selling refers to instances where banks, insurers, funds, asset managers or financial brokers sell overly complex, expensive or illiquid products that may not meet client suitability requirements. Customer relations risks could damage an entity's customer base, brand, reputation and earnings potential and can also result in fines and legal claims.

B. (ii) Human Capital

The recruitment, training & retention of skilled and experienced employees are pivotal for entity's financial performance and reputation. The presence of unfavorable labor relations and rigid workforce provisions may indicate inherent exposure to labor relations risk. The inability of the issuers' to reduce staff or costs during an economic downturn, challenges in attracting & retaining people with required skills or productivity loss due to strikes may affect earnings negatively. External or internal perceptions of a lack of diversity or a hostile culture may lead to reduced productivity, lawsuits or may hurt an enterprise's ability to attract employees.

Relevant considerations may include the impact of working days lost due to strikes, fines related to labor regulations, track record of successfully negotiating wage agreements and relationship with unions. Adherence to wage agreements, effective negotiations with employees' representatives and a strong monitoring framework to ensure compliance may minimize disputes. The presence of safe & secure working environment, acknowledgement of merit with respect to education & experience and an equal opportunity employer opportunities that encourages inclusive culture as reflected in religious, ethnic & gender diversity are pivotal to enhance human capital performance. Partnerships with educational institutions may facilitate a dependable supply of workers. Comprehensive hiring and promotion policies may facilitate a diverse and inclusive workplace, which may attract talent. Arrangement of retirement benefits for employees including provident fund, gratuity etc. may facilitate in retention of quality human capital thereby increasing productivity. Prevention of child labor and human rights abuse at work place reduces human rights violations & penalties.

The recruitment and retention of highly specialized professionals is also important for financial institutions. Effective policies to attract and retain skilled employees and to maintain constructive staff relations may minimize disputes & disruptive employee actions and help a financial institution to focus on business objectives easily. External or internal perceptions of a lack of diversity, equity including gender discrimination and unequal compensation structures may lead to reduced productivity, lawsuits or may hurt a financial institution's ability to attract skilled employees. Abstain from undertaking transactions that may have any adverse social implications on the society or utmost care to understand and assess the use of products & services by the customers preserve the institutions' reputation and prevents from penalties and lawsuits.

B. (iii) Demographic And Societal Trends

Changing demographics, consumer preferences or societal trends including government policies may affect an issuer's earnings and long term sustainability. An issuer's reliance on a narrow or shrinking demographic base for sales may indicate inherent risk exposure. Similarly, some products or services like medical care or utilities are more vulnerable to societal or governmental pressure than other sectors because access to these products and services at an affordable price has broad ramifications for social cohesion.

Entities in regulated sectors may be particularly exposed to socially driven policy agendas that can significantly change their business and financial requirements. Regulatory and legislative changes may advantage or disadvantage entities based on the societal trends. Demand or access to capital may decline for enterprises that sell products or services misaligned with social expectations in the markets.

Customer awareness of an organization's business practices as well as its products or service may also influence demand and public perception. Geographic and product diversity as well as ability to quickly adapt to consumer preferences, regulatory changes and societal trends may help mitigate risk or lead to competitive advantages.

Both demographic and societal trends may affect financial institutions' revenue and earnings as well as the way they do business and offer products. Geographic and product diversity as well as ability to quickly adapt to consumer preferences, regulatory changes and societal trends help mitigate these risks or lead to competitive advantages.

Changing demographics require financial institutions to adjust to the financial lifecycles of their customers and offer financial products that fulfil the requirement of the diversified customer base. Societal trends create opportunities to expand in the market but also present challenges. For example, regulatory or policy effort to increase customer base at capped rates may render some business lines uneconomic, otherwise the institution perceived to be misaligned with social expectations may experience restricted access to capital. In extreme cases, regulatory or policy actions may even threaten an entity's viability.

B. (iv) Health And Safety

Employees and contractors encounter health and safety issues at the work place. These issues are important because accidents may generate negative publicity and disrupt operations. Regulatory pressure for safe working environment may result in higher costs as unsafe environment may lead to increased labor costs, labor shortages, higher operations downtime and necessary more investment in training employees.

Enterprises that involve heavy equipment and machinery, handling of hazardous materials and dangerous operating conditions generally have higher exposure to health and safety risk than an enterprise that relies on knowledge workers. Relevant considerations may include fatality and injury rates, working hours lost due to unsafe operational activities and number of safety failings.

Entities may offset health and safety risk through compliance with health & safety regulations and through advances in technology & monitoring equipment. Societies generally expect employers to maintain a safe workplace, so its health and safety practices are important and can have significant positive or negative impact on its sales and reputation. The entities that provide proper health & medical benefits to employees have positive impact on their reputation and are considered socially responsible entities.

Financial institutions typically have low exposure to health and safety risks because they rely on knowledge workers and typically do not expose their employees to the handling of hazardous materials or dangerous operating conditions. More relevant health and safety risks for financial institutions relate to employee mental health and well-being which may impact productivity and the broader reputation of the institution. Financial institutions can mitigate this risk by nurturing a health and safety conscious culture through management & employees training & support and through compliance with both internal & regulator's policies and regulations.

B. (v) Responsible Production

Responsible production incorporates the risks and opportunities of how an issuer manages its production processes, supply chain or delivery of services. These also include the impact of product failures, recalls, contaminations and violations. A well-established reputation for high product quality may create a competitive advantage whereas product failures may lead to a damaged reputation with suppliers, customers and regulators. The potential harm related to the use of end product or service may indicate inherent risk exposure and may be mitigated by adherence to manufacturing and safety standards.

Supply chain management is key to enterprise's success as weaknesses in this area can lead to supply disruption, increased costs or reputational damage for the issuer. Enterprises may be able to mitigate supply chain risk through diversification of the supplier base to ensure alternative suppliers in case of supply disruptions or disputes. An enterprise's framework for managing multiple suppliers with focus on diversity, resilience, reputation and cost efficiency can be relevant considerations. Management should continuously check the suppliers' adherence to ESG compliance and should have stringent SOPs for filtering suppliers not adhering to best practices.

Entities depend on the communities for their workforce in the areas they operate, so their engagement with those communities may affect their ability to attract and retain employees as well as their revenues. Positive community relationships and comprehensive due diligence that considers potentially positive and negative effects of new investment decisions on the community may help to offset risk. Poor relationships can hinder Greenfield investment projects or raise potential execution challenges. Statements from community leaders, the effectiveness of an enterprise's media strategy and evidence of stakeholder engagement policies may be relevant considerations.

Responsible production refers to the creation of financial products that suitably meet customer needs and the appropriateness of business practices in which financial institutions engage in their day-to-day operations. Financial products designed to address client needs without undue complexity and risk reduce an institution's exposure to reputational risk and litigation. The design of complex or speculative financial products increases the risk of product failures for the institution and their clients leading to social repercussions such as economic losses. Similarly, facilitation of illegal activities such as money laundering, bribery, corruption or engaging in sensitive activities such as tax optimization can negatively impact a financial institution's reputation and result in regulatory penalties.

C. GOVERNANCE RISK ("G")

Governance risks are an important consideration for all debt issuers. Unlike environmental and social risks, which may be driven by external factors, governance risks are largely issuer driven. Governance relates to the framework and processes through which decisions are made and related actions are carried out. The different constituents of governance help direct and manage business and financial activities.

We broadly classify governance risks that are generally most relevant from a credit perspective into five categories: (i) financial strategy and risk management; (ii) management credibility and track record; (iii) organizational structure; (iv) compliance and reporting; (v) board structure, policies and procedures.

Financial Strategy & Risk Management	Management Credibility & Track Record	Organizational Structure	Compliance & Reporting	Board Structure, Policies & Procedures

C. (i) Financial Strategy And Risk Management

Financial strategy and risk management policies reflect the enterprise's tolerance for risk which directly affects debt & equity levels, financial planning and future direction. Entity's board has a critical role in the area of risk management which includes development of risk management framework, setting & monitoring the enterprise's risk appetite and policies protecting the interests of all stakeholders including creditors. Relevant considerations may include an issuer's desired capital structure, CAPEX planning, dividend policy and its history of prior actions related to financial strategy and risk management. Management compensation is an indication of how an enterprise's compensation structure might encourage excessive risk-taking. A commitment to a conservative credit profile and strong liquidity may support enterprise in economic downturn and provide comfort for its creditors but limits the potential upside when economy is burgeoning. On the other hand, a highly leveraged capital structure focus on shareholders at the expense of creditors indicate high risk tolerance. The use of cash during different economic and industry cycles and the enterprise's response to key events such as economic downturn, competitive challenges or regulatory pressure may indicate enterprise's risk appetite.

Financial institution's risk-taking capacity and its risk appetite drives its financial strategy and the long term sustainability of its investments, lending, underwriting and product offerings. Risk culture and risk management framework are key drivers of a financial institution's credit quality. A comprehensive risk governance framework fully embedded in an institution's culture improve operational effectiveness and lowers risk.

A commitment to a high level of capitalization, diversified lending and strong liquidity often indicates a strong governance. A well-developed risk management framework of financial institutions is embedded in multiple layers of the organization, for example, (i) business lines manage the risks; (ii) risk management functions provide policies, frameworks and procedures and independently measure, monitor and report risk on an enterprisewide basis; (iii) an internal audit function reports on the effectiveness of the risk governance framework and adherence to policies and procedures.

On the other hand, deficiency of proper risk management and compliance policies or frequent breaches are indicators of weak corporate governance. This could lead to a deterioration in investing, lending or underwriting discipline. Business complexity increases risk management challenges and the need for sophisticated risk management and robust governance. Examples include exposure to opaque illiquid assets, obscure counterparties, or complex derivatives and financial products.

C. (ii) Management Credibility And Track Record

The credibility and track record of management help achieve its target credit profile & operational goals and may provide insight into future performance of the enterprise. Relevant considerations include management's track record for meeting goals and variability of operating results during periods of market fluctuations. Enterprises that consistently set and meet its goals, maintain target credit profile during economic downturns and anticipate market conditions have a track of greater management credibility.

Significant shifts in strategy, for example entering a new business line or geographic region where management has limited experience can increase risk. Consistent achievement of synergies from business integration and a successful expansion may indicate management's ability to manage risk effectively. Management's ability to strategize in response to changing industry and market conditions or its failure to do so may be a relevant consideration. High executive turnover or dependence on one individual or a group of executives can pose risk to management credibility especially in the absence of a succession plan. For some enterprises, success in managing regulatory relationships may be a relevant consideration particularly where a sector requires approvals or permits from government or other agencies.

The credibility and track record of financial institution's management for executing the strategy agreed by the board and the volatility of operating results are relevant considerations to form opinion about their ability to achieve its financial goals and provide valuable insight for its future performance. An institution that has a track record of anticipating and adapting to evolving business or market conditions generally demonstrates strong management.

The transparency and consistency of management communication and actions are also relevant considerations. Management with extensive experience in managing the business through economic and credit cycles typically has a better understanding of risks and opportunities. Significant shifts in strategy, shake-up in management, poor succession planning or inexperience management team can all indicate weaknesses in a financial institution's governance.

C. (iii) Organizational Structure

Organizational structure is unlikely to materially improve the credit profile of an issuer but may create risk if significant cross-shareholdings in group companies or frequent changes in organizational structure obscure performance or create conflict of interest. An ownership structure that blurs the financial separation of parent or holding entities within the group and lacks protection from restricted payments covenants can lead to poor financial transparency and exposes creditors to cash leakage.

Parent or holding companies with multiple subsidiaries that also hold voting rights in the parent or other subsidiaries or that can transfer financial obligations to other subsidiaries may create risk. Relationship between parents and subsidiaries, related party transactions rules, policies governing the flow of funds between entities may be relevant considerations for evaluation of organizational structure.

Organizational structure may expose the financial institutions to governance risks and hinders the capacity to fully assess risk. Complex subsidiary structure or offshore holding companies may decrease the visibility of risks. Managing multiple business lines across various geographies under different tax, legal and regulatory regimes increase complexity and risk. Related-party transactions may indicate a governance weakness and financial institutions that extend credit to insiders in the form of related-party transactions can create conflicts of interest, reputational damage and impair the ability to get further deposits or external financing.

C. (iv) Compliance and Reporting

A relatively good financial performance does not necessarily warrant presence of good governance in an entity. The timely provision of information and transparency in disclosures allows all stakeholders to make informed decisions and is considered an overriding necessity. The corporate governance practices implemented by the management to achieve transparency, accountability & fair play, its benchmarking against global best practices and protection of rights of all stakeholders may be the relevant considerations. The timeliness and accuracy of required disclosures are also important for issuers because a qualified audit opinion may indicate higher governance risk that could result in a potential default under debt agreements. Non-reporting of required disclosures may also result in any regulatory or legal actions against the enterprise. The timeliness, transparency and comprehensiveness of financial statements, audit opinions (qualified or non-qualified), frequent changes in auditors and auditor comments regarding the quality of internal controls may be the relevant considerations.

In case of legal actions against the enterprise, considerations may be given to a judgment or penalty which is likely to affect issuer's access to capital markets, its competitive position, reputation and the level of management involvement. For all compliance and reporting risks, efficacy of corrective measures and the likely timeline to resolution may be the relevant considerations. Removal of top management related to compliance and reporting issues may point to a weak governance.

Strong compliance and control functions along with timeliness & accuracy of reporting are principal aspects of governance for all financial institutions. Compliance and reporting issues including know-your-customer & money laundering failings expose institutions to regulatory actions, financial penalties and prolonged regulatory investigations. In case of a regulatory breach, considerations may be given to a judgment or penalty which is likely to affect an issuer's reputation, access to capital markets, loss of license or consequent inability to operate the business.

Consideration may also be given whether the breach is due to an operational issue, a wider governance failure or an intentional management decision as well as the remedial actions in response to the breach. For all compliance and reporting issues including incidents of corruption, effectiveness of corrective measures undertaken and the timelines to resolution may be relevant considerations.

Financial institutions may also be reviewed for adoption of ethical practices. Relevant considerations may be responsible lending procedures and due diligence of financial flexibility of the customer that inhibits overburdening an already highly leveraged borrower. The gain of market share in a highly competitive environment while functioning as an ethically responsible entity and the protection of depositors' rights may also be relevant considerations.

C. (v) Board Structure, Policies and Procedures

Boards' oversight and effectiveness are important because boards perform a role in the oversight of risk management, setting and monitoring risk appetite and risk management framework. Ownership concentration, degree of control and protection given to different stakeholders may be relevant considerations.

The design of management compensation policy typically set by the board may also affect the enterprise's credit profile depending on the incentives (e.g., short-term vs long-term incentives). If pay and compensation structures are not aligned with sustainable operating performance or incentivize short-term aggressive growth outcomes over stable credit profile, such policies may encourage excessive risk-taking that negatively impacts creditors. Board's composition, Directors' independence, levels of relevant experience, succession planning, board turnover and diversity may be relevant considerations when assessing overall board oversight.

Boards in financial institutions perform a critical role in the supervision of management, strategy, business operations, setting & monitoring of risk appetite and its risk management framework. The board's risk committee is important because it sets the risk appetite, oversees the policies and procedures that establish risk controls, approves and monitors overall risk limits and drives risk culture.

Board's composition, directors' independence, relevant experience, diversity, succession planning and turnover are relevant considerations in assessing overall board effectiveness. Boards with concentrated ownership increases the risk of imprudent business practices such as transactions with related parties not at an arm's length basis. Concentrated ownership or control may also render a board's independent oversight more difficult. The board must manage the conflicts of interest prudently at arm's length without compromising the interests of controlling shareholders and those of other stakeholders including minority shareholders.

RATING SCALE & DEFINITIONS

Rating scale and Definitions may be accessed at (https://docs.vis.com.pk/docs/VISRatingScales.pdf)

Faheem Ahmad

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Mr. Ahmad possesses 30+ years experience in financial risk assessment with focus on Islamic finance, venture capital and general management. He has top level management experience at international level in the fields of credit ratings, Islamic and conventional financial risk assessment modeling, industrial management and construction engineering. Mr. Ahmad is an active participant at international forums on Credit Ratings. He obtained his B.S in Civil Engineering from NED University of Engineering and Technology, Karachi. He also has Masters Degrees in Engineering and Business Administration from USA.

Muhammad Abu Bakar

Group Head - Business Development

Muhammad Abu bakar graduated from University of Engineering & Technology, Lahore in Dec 2000 with a Bachelors in Chemical Engineering. He also holds a Master's degree in Business Administration from Lahore University of Management Sciences, June 2006. He begin his professional career from Dawood Hercules Chemicals as a trainee engineer for a year. Later, he joined Nimir Chemicals Pakistan Limited as an Assistant Production Manager, where he handled production and planning activities of the plant, for a period of two years. He worked in UBL as a Risk Analyst and worked there for about more than a year, carrying out credit analysis of commercial clients of the bank. In Jan 2008, he joined Standard Chartered Bank as a Relationship Manager and fulfilled the role of business development of their corporate clients. In June 2011, he got a chance to join Dubai Islamic Bank as a Unit Head Credit Approval and held the responsibility of credit evaluations and approvals for corporate clients of the central region. In Oct 2018, Abu bakar joined VIS Credit Rating Company Limited as a Group Head Business Development-North.

Jahangir Kothari Parade (Lady LLoyd Pier) Inspired by Her Excellency, The Honorable Lady Lloyd, this promenade pier and pavillion was constructed at a cost of 3 Lakhs and donated to the public of Karachi by Jahangir Kothari to whose genrosity and public spirit the gift is due. Foundation stone laid on January 5, 1920. Opened by Her Excellency, The Honorable Lady Lloyd on March 21, 1921.

Dome: A roof or vault, usually hemispherical in form. Until the 19th century, domes were constructed of masonry, of wood, or of combinations of the two, frequently reinforced with iron chains around the base to counteract the outward thrust of the structure.

Origins: The dome seems to have developed as roofing for circular mud-brick huts in ancient Mesopotamia about 6000 years ago. In the 14th century B.C. the Mycenaean Greeks built tombs roofed with steep corbeled domes in the shape of pointed beehives (tholos tombs). Otherwise, the dome was not important in ancient Greek architecture. The Romans developed the masonry dome in its purest form, culminating in a temple built by the emperor Hadrian. Set on a massive circular drum the coffered dome forms a perfect hemisphere on the interior, with a large oculus (eye) in its center to admit light.

VIS Credit Rating Company Limited is committed to the protection of investors and offers a blend of local expertise and international experience to serve the domestic financial markets. With its international reach, VIS is positioned to aim for an international mark. In this regard, the global experience of our international affiliates and partners have been invaluable towards adding depth to our ongoing research endeavors, enriching us in ways, that enable us to deliver our responsibilities to the satisfaction of all investors. The edifice of the Jahangir Kothari Parade has stood proudly through the years and is a symbol of our heritage. Its 'Dome' as the most stable of building structures, exemplifies architectural perfection. Committed to excellence, VIS continues its endeavour to remain an emblem of trust.

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