

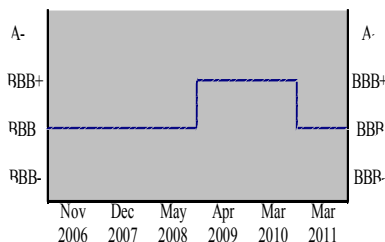


RATINGS (APRIL 2011)
NETWORK MICROFINANCE BANK LIMITED (NMBL)

	NEW*	PREVIOUS
Long Term	BBB	BBB+
Short Term	A3	A2

* These ratings are placed on Rating Watch.

LONG-TERM RATING HISTORY



FINANCIAL DATA

PKR (mln)	2010	2009	2008
Advances	61.6	92.0	68.8
Total Assets	251.9	351.4	193.1
Deposits	29.0	110.9	101.3
Equity	220.1	238.6	88.3
Net Interest Income	45.3	45.4	25.3
Net Non-Performing Loans**	20.0	15.1	6.2
Net income	(18.4)	0.3	(16.0)

** Net of Provisions

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RATING RATIONALE AND KEY DRIVERS

- The ratings reflect significant squeeze in business operations of NMBL, mainly on account of increase in non-performing loans, low deposit base, and minimal operating margins; thereby, subdued performance prospects. The ratings recognize the bank's concentrated business operations, persistent inflationary pressure on micro-borrowers, and deteriorating socio-economic factors impacting the sector. Nevertheless, while meeting capitalization requirements, the bank maintains strong liquidity profile and has adopted a cautious stance towards credit expansion. The bank's major sponsor – Jahangir Siddiqui & Company Limited – has decided to divest its ownership. Pending finalization of the transaction, the ratings of the bank are placed on Rating Watch.
- The ratings are dependent upon the bank's ability to arrest rising trend in NPLs, while building a quality loan book to improve its earning prospects. At the same time, strengthening of risk management procedures and control mechanism, supplemented by vigilant post disbursement monitoring of loans would remain important. In addition, persistent pressure on the bottom-line, in turn impacting risk absorption capacity of the bank, may have negative implications for the ratings.

ASSESSMENT

- Microfinance sector of Pakistan, despite setbacks, has grown 19% during 2010 with total micro portfolio standing at PKR 25bln. However, the profitability and key performance indicators remained weak. Most of the microfinance lenders were affected by the devastating floods in the country during 2HCY10. In addition, socio-economic conditions including high inflation, power shortages and security concerns have hampered the repayment ability of the micro borrowers. Currently, NMBL has 5,734 clients with an average loan size of PKR 10,746 (at end-Dec10). The bank's primary customers are micro-entrepreneurs, who require financial assistance to sustain business activities.
- During latter part of 2010, Network Microfinance Bank experienced sizeable reduction in its earning assets to PKR 215mln (2009: PKR 298mln). The bank's loan book significantly squeezed owing to the management's decision to stop lending subsequent to substantial increase in non-performing loans. Although, the management also shed high cost deposits, it remains confident to mobilize the funds once need arises. Increase in NPLs has been due to diminishing earning capacity of borrowers owing to deteriorating economic fundamentals in general and worsened law and order situation in areas of Karachi, where the bank operates, in particular. Consequently, the management focused to consolidate its existing loan book while pursuing recoveries of delinquent loans.
- The bank posted a net loss during 2010, mainly on account of high provisioning expense of PKR 19.2mln (2009: PKR 2.9mln). Net interest income remained largely on the same level. However, the bank witnessed decrease in its spreads because of change in asset mix in favor of low yielding, though low risk, Govt. securities. During 1Q11, the bank posted a net loss of PKR 3.4mln mainly on account of provisioning expense.
- Going forward, while the bank intends to focus on recoveries, contraction in performing loans portfolio is expected to keep the profits in check. However, relatively higher investment in Govt. securities would lend some support to the bottom-line. Meanwhile, improvement in revenues and sustainability of the same would depend on the ability of the management to develop quality income streams. While the consolidation phase is expected to continue for most of 2011, the bank is expected to further strengthen its operational framework before it starts fresh lending latter in the year.
- The bank registered significant squeeze in its deposit base (2010: PKR: 29mln, 2009:110mln). The majority of the bank's operations are presently funded through equity. The deposit base of the bank remains highly concentrated with the top ten depositors comprising around 68% of total deposits as on end-Dec10.
- The bank's asset quality has deteriorated substantially as impaired lending increased by 67%. Consequently, the management has put its lending business on hold while making efforts to recover delinquent loans. However, the rise to this high level of NPLs highlighted the need for review of the bank's credit identification, disbursement and monitoring framework. The management remains hopeful that the recovery efforts would improve NMBL's financial profile, going forward.
- NMBL meets regulatory minimum capital requirement for district level. With the bank's high capital adequacy ratio and low Net NPLs to equity, overall capital base would likely to sustain at current level. However, any significant bottom-line loss owing to either decline in earning capacity of the bank or further provisioning requirement may result in non-compliance with capitalization requirement (end2011: PKR 200mln, end2012: PKR 250mln) besides a decline in risk absorption capacity of the bank.

PROFILE:

- NMB, established under the Microfinance Institution Ordinance 2001, is listed on Karachi Stock Exchange. Started in 2005, it operates at the district level in Karachi. The key sponsor of the bank is Jahangir Siddiqui & Co. Limited (JSCL) with around 71% holding. However, JSCL is in the process of divesting its entire holding in the bank.
- Mr. Zainul Abidin Memon, President & Chief Executive, has joined the bank in September 2010. He is an experienced banker with over four decades of banking experience. He is supported by a team with adequate experience in the microfinance sector.