



The Pakistan Credit Rating Agency Limited

## GUARANTCO LIMITED

	<b>NEW</b> [SEP-17]	<b>PREVIOUS</b> [JAN-17]
Long-Term	AAA	AAA
Short-Term	A1+	A1+
Outlook	Stable	Stable

<b>REPORT CONTENTS</b>
1. RATING ANALYSES
2. FINANCIAL INFORMATION
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<p><b>Profile &amp; Ownership</b></p> <ul style="list-style-type: none"> <li>Joint Venture Financial Institution with international operations.</li> <li>Established with the mandate to support infrastructure projects in low income countries via guarantee provisions and development of local financial debt markets.</li> <li>Shareholders are five highly rated sovereigns - United Kingdom (AA by S&amp;P), Switzerland (AAA by S&amp;P), Sweden (AAA by S&amp;P), and Australia (AAA by S&amp;P) own 71%, 11%, 6%, and 1% respectively through The Private Infrastructure Development Group (PIDG) and Netherlands (AAA) owns 11% through FMO.</li> <li>PIDG with consolidated strength of eight members is a donor financed trust while FMO is a development bank (51% owned by the Dutch government through Dutch Ministry of Foreign Affairs).</li> <li>Capital injections by sponsors on continuous basis signifying commitment to support.</li> </ul> <p><b>Governance</b></p> <ul style="list-style-type: none"> <li>Seven member experienced board comprising non-executive directors chaired by Mr. Andrew Brainbridge.</li> <li>Selection of the board is made by a public tender process. Board members are selected by a panel that has representatives from the donors.</li> <li>Close monitoring and oversight of management, guarantee portfolio, and investments is ensured through committees.</li> </ul> <p><b>Management</b></p> <ul style="list-style-type: none"> <li>Management of guarantee portfolio is outsourced to GuarantCo Management Limited (GMC), a fully owned subsidiary of Cardano Development. The contract with the previous management, Frontier Markets Fund Managers (FMFM) ended on 8<sup>th</sup> May 2016.</li> <li>Treasury investment book is subcontracted to PIMCO and Fidelity.</li> <li>Mr. Lasitha Perera; the CEO took over the position in Jan17. He is an experienced investment banker indirectly associated with the company since 2009.</li> </ul> <p><b>Risk Management</b></p> <ul style="list-style-type: none"> <li>Established risk management policies.</li> <li>Diversified guarantee portfolio with identified exposure limits.</li> <li>High credit risk – Guarantee portfolio focused towards countries below investment grade as per mandate.</li> <li>Provision for currency risk incorporated in measuring guarantee capacity.</li> <li>During 1HCY17, the overall quality of asset book improved (Infection ratio: 1HCY17:13.1%; CY16: 11.2%; CY15: 13.1%; CY14: 5.8%).</li> </ul> <p><b>Performance</b></p> <ul style="list-style-type: none"> <li>Two revenue streams: (i) guarantee income and (ii) investment portfolio.</li> <li>Increased income from both avenues resulted in rise in gross revenues (1HCY17: USD 5.3mln; CY16: USD 14.6mln; 1HCY16: USD 7.5mln; CY15: USD 13.3mln; CY14: USD 9.5mln).</li> <li>During CY16, one-time management contract cancellation fee paid to FMFML of USD 3mln caused a pre-provisioning loss of USD 1.1mln (CY15: USD +0.4mln; CY14: USD +1.3mln).</li> <li>Net finance income from funds dipped though it is cushioned by fair value profit on financial assets.</li> <li>During 1HCY17, in absence of any major expense pre provisioning loss rest at USD 1.4mln (1HCY16: USD 2.5mln).</li> <li>Provisioning expense in CY16 of USD 2.1mln increased net loss to USD 3.2mln. (Provisioning expense – CY15: USD 6.4mln; CY14: USD 10.6mln); (Net loss - CY15: USD 6mln; 9MCY15: USD 5.8mln CY14: USD 9.3mln).</li> <li>During 1HCY17, bottom-line rest at USD 1.3mln (1HCY16: USD 3.4 mln) mainly owing to reversal in provisions.</li> <li>Improvement in quality of underperforming portfolio – a major challenge.</li> <li>Almost half of GuarantCo's revenue comes from Africa as per its mandate, with additional focus Asia going forward, supported by increasing outreach.</li> <li>Target of increasing the guarantee portfolio to USD 1bn by end-2020.</li> </ul> <p><b>Financial Facilities</b></p> <ul style="list-style-type: none"> <li>Strong liquidity profile (Liquid assets/ Gross guarantees – 1HCY17: 83.9%; CY16: 90.6%; CY15: 99.2%; CY14: 109.3%).</li> <li>Robust capitalization as evident by capital to guarantee portfolio ratio (1HCY17: 1.1x; CY16: 1.2x; CY15: 1.3x; CY14: 1.3x).</li> <li>In CY16, the counter-guarantors facility of USD 450mln from KFW through FMO was cancelled and replaced with callable capital facility of USD 50mln (GBP 40mln) from UK (DFID). This facility was finalized with DFID in CY16 and used in Jan 17.</li> <li>FMO has also provided a standby facility of USD 30mln, which, when called, will be converted into debt. This was also finalized in CY16.</li> <li>During July 17, Australian government's Department of Foreign Affairs and Trade (DFAT) provided further AUD 4mln (CY15: AUD 4mln) donation for continued growth of organization.</li> </ul>	<p><b>RATING RATIONALE</b></p> <p>GuarantCo Limited, an international Joint Venture development financial institution, is directly and indirectly owned by five highly rated sovereigns. Continuous sponsors support is evident from injections by Australian government's Department of Foreign Affairs (DFAT) and callable capital from the UK via PIDG. GuarantCo mainly operates in low income, below investment grade countries. Its objective is to facilitate flow of debt capital to projects having bearing on infrastructure and a positive long term impact by offering credit guarantees.</p> <p>GuarantCo is cautiously building its guarantee portfolio with adequate emphasis on diversification: geographical, entity and sector. More than 60% of the company's portfolio is tilted to Africa, although GuarantCo is focusing to gain more exposure in Asia supported by their recently opened office in Singapore. There is almost 13% impairment in the quality of guarantee assets. However, given the small size, this might be reflective of otherwise detailed and robust credit evaluation and monitoring framework.</p> <p>The Company maintains good provision coverage. During 1HCY17, whilst a significant decrease in investment income was witnessed, the overall return on investment remained positive as a result of the fair value of the investments. Provisioning reversals supported reduction in loss. Meanwhile, the sponsors gradually injected fresh funds to keep the company equipped with robust capitalization. A healthy treasury investment portfolio mainly comprising fixed income corporate bonds and US Treasury funded by its equity. Thus liquidity stayed strong along with sizable income stream. GuarantCo Management Company, a fully owned subsidiary of Cardano Development, is fund manager; responsible for commercial operations of GuarantCo. The contract has been assigned for relatively a longer period which is expected to help the management, to pursue a well-conceived strategy to achieve profitability in the near term. Nevertheless, the management's success in achieving its business objectives while capitalizing on its identified niche – infrastructure development remains to be seen.</p>
	<p><b>KEY RATING DRIVERS</b></p> <p>GuarantCo's ratings are dependent on its robust ownership structure, well supported by implicit indeed demonstrated commitment by the sponsors. The Company's ability to achieve desired growth in its guarantee portfolio is important to pull off from bottom line losses. Meanwhile, close monitoring of asset quality remains critical.</p>



GuarantCo Limited

Balance Sheet	30-Jun-17 1HCY17	31-Dec-16 CY16	31-Dec-15 CY15	31-Dec-14 CY14
<b>ASSETS</b>				
<b>Earning Assets</b>				
1. Deposits with Banks	46,084	46,250	41,927	72,864
2. Investments	215,930	213,442	213,289	197,702
Trade and other receivables	14,207	13,712	3,805	3,284
Deferred expenses	71	-	1,657	2,181
Deferred Tax	-	-	48	115
<b>TOTAL ASSETS</b>	<b>276,292</b>	<b>273,404</b>	<b>260,727</b>	<b>276,145</b>
<b>LIABILITIES</b>				
<b>Current Liabilities</b>				
1. Derivative Financial Instruments	501	-	7,475	5,843
2. Trade and other payables	2,685	2,688	4,964	6,790
3. Provision - Guarantee payable	10,685	10,194	7,276	20,487
Deferred Income	4,910	4,855	3,039	1,796
<b>EQUITY</b>				
<b>TOTAL EQUITY</b>	<b>257,511</b>	<b>255,668</b>	<b>237,973</b>	<b>241,230</b>
<b>TOTAL LIABILITIES &amp; EQUITY</b>	<b>276,292</b>	<b>273,404</b>	<b>260,727</b>	<b>276,145</b>
<b>INCOME STATEMENT</b>				
Guarantee Revenue	4,204	8,207	6,692	4,555
Investment Income	1,142	6,380	6,635	4,961
Fund Manager Fee & Administrative expenses	(5,288)	(11,377)	(9,910)	(7,421)
Grant expense	(430)	(850)	(418)	(336)
Operating Profit	(1,513)	(4,019)	(3,636)	(3,201)
Provisions w.r.t guarantees	43	(2,114)	(6,375)	(10,618)
Net Finance Income	1,142	6,380	6,635	4,961
Taxation	(23)	(59)	(79)	(19)
<b>Net Income</b>	<b>(1,393)</b>	<b>(3,286)</b>	<b>(6,051)</b>	<b>(9,292)</b>
<b>RATIO ANALYSIS</b>				
<b>Ratio Analysis</b>				
<b>Profitability Ratios</b>				
1. ROE	-1.1%	-1.3%	-2.5% *	-4.4%
<b>Liquidity Ratios</b>				
1. Liquid Assets/Gross Guarantees	83.9%	90.6%	99.2% *	119.2%
2. Liquid Assets/Equity	101.7%	101.6%	107.2% *	112.2%
<b>Guarantee Loss Coverage</b>				
1. Stressed Assets Coverage Stressed Assets Coverage (Provisions/Stressed Assets)	44.1%	44.1%	44.1%	100.0%
2. Infection Ratio (Impaired Guarantees / Gross Guarantees)	13.1%	11.2%	13.1%	5.8%
<b>Capital Adequacy</b>				
1. Equity/Total Assets	97.0%	97.1%	93.9%	94.4%
2. Equity/Gross Guarantees	82.4%	89.2%	92.5%	106.2%

GuarantCo Limited

Sep-17

## CREDIT RATING SCALE & DEFINITIONS

Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

<b>LONG TERM RATINGS</b>		<b>SHORT TERM RATINGS</b>
<b>AAA</b>	<b>Highest credit quality.</b> Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments.	<p><b>A1+:</b> The highest capacity for timely repayment.</p> <p><b>A1:</b> A strong capacity for timely repayment.</p> <p><b>A2:</b> A satisfactory capacity for timely repayment. This may be susceptible to adverse changes in business, economic, or financial conditions.</p> <p><b>A3:</b> An adequate capacity for timely repayment. Such capacity is susceptible to adverse changes in business, economic, or financial conditions.</p> <p><b>B:</b> The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions.</p> <p><b>C:</b> An inadequate capacity to ensure timely repayment.</p>
<b>AA+</b>	<b>Very high credit quality.</b> Very low expectation of credit risk.	
<b>AA</b>	Indicate very strong capacity for timely payment of financial commitments. This capacity is not significantly vulnerable to foreseeable events.	
<b>AA-</b>		
<b>A+</b>	<b>High credit quality.</b> Low expectation of credit risk.	
<b>A</b>	The capacity for timely payment of financial commitments is considered strong. This capacity may, nevertheless, be vulnerable to changes in circumstances or in economic conditions.	
<b>A-</b>		
<b>BBB+</b>	<b>Good credit quality.</b> Currently a low expectation of credit risk.	
<b>BBB</b>	The capacity for timely payment of financial commitments is considered adequate, but adverse changes in circumstances and in economic conditions are more likely to impair this capacity.	
<b>BBB-</b>		
<b>BB+</b>	<b>Moderate risk.</b> Possibility of credit risk developing.	
<b>BB</b>	There is a possibility of credit risk developing, particularly as a result of adverse economic or business changes over time; however, business or financial alternatives may be available to allow financial commitments to be met.	
<b>BB-</b>		
<b>B+</b>	<b>High credit risk.</b>	
<b>B</b>	A limited margin of safety remains against credit risk. Financial commitments are currently being met; however, capacity for continued payment is contingent upon a sustained, favorable business and economic environment.	
<b>B-</b>		
<b>CCC</b>	<b>Very high credit risk.</b> Substantial credit risk	
<b>CC</b>	“CCC” Default is a real possibility. Capacity for meeting financial commitments is solely reliant upon sustained, favorable business or economic developments. “CC” Rating indicates that default of some kind appears probable. “C” Ratings signal imminent default.	
<b>C</b>		
<b>D</b>	Obligations are currently in default.	

**Outlook (Stable, Positive, Negative, Developing)**  
Indicates the potential and direction of a rating over the intermediate term in response to trends in economic and/or fundamental business/financial conditions. It is not necessarily a precursor to a rating change. ‘Stable’ outlook means a rating is not likely to change. ‘Positive’ means it may be raised. ‘Negative’ means it may be lowered. Where the trends have conflicting elements, the outlook may be described as ‘Developing’.

**Rating Watch**  
Alerts to the possibility of a rating change subsequent to, or in anticipation of, a) some material identifiable event and/or b) deviation from expected trend. But it does not mean that a rating change is inevitable. A watch should be resolved within foreseeable future, but may continue if underlying circumstances are not settled. Rating Watch may accompany Outlook of the respective opinion.

**Suspension**  
It is not possible to update an opinion due to lack of requisite information. Opinion should be resumed in foreseeable future. However, if this does not happen within six (6) months, the rating should be considered withdrawn.

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A rating is withdrawn on a) termination of rating mandate, b) cessation of underlying entity, c) the debt instrument is redeemed, d) the rating remains suspended for six months, e) the entity/issuer defaults, or/and f) PACRA finds it impractical to surveil the opinion due to lack of requisite information

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**Name of Rated Entity**  
**Sector**  
**Type of Relationship**

GuarantCo Limited  
 International DFI  
 Solicited

**Purpose of the Rating**

Independent Risk Assessment

[Rating History](#)

Date	Long Term	Short Term	Outlook	Rating Watch
29-Sep-17	AAA	A1+	Stable	-
13-Jan-17	AAA	A1+	Stable	-
13-Jan-16	AAA	A1+	Stable	-

**Related Criteria and Research**

**Rating Methodology**

Bank Rating Methodology

**Sector Research**

Credit Guarantee Institutions | Jan17

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[Rating Team Statement](#)

**Rating Procedure**

Rating is an opinion on relative credit worthiness of an entity or debt instrument. It does not constitute recommendation to buy, hold or sell any security. The rating team for this assignment does not have any beneficial interest, direct or indirect in the rated entity/instrument.

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[Probability of Default \(PD\)](#)

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