The Pakistan Credit Rating Agency Limited

Rating Report

Apna Microfinance Bank Limited

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
29-Apr-2023	BBB+	A3	Negative	Maintain	Yes
30-Apr-2022	BBB+	A3	Negative	Maintain	Yes
30-Apr-2021	BBB+	A3	Stable	Maintain	Yes
30-Apr-2020	BBB+	A3	Stable	Maintain	Yes
30-Oct-2019	BBB+	A3	Stable	Maintain	-
30-Apr-2019	BBB+	A3	Stable	Maintain	-
04-Dec-2018	BBB+	A3	Stable	Maintain	-
28-May-2018	BBB+	A3	Stable	Upgrade	-
10-Nov-2017	BBB	A3	Stable	Maintain	-
10-May-2017	BBB	A3	Stable	Downgrade	-

Rating Rationale and Key Rating Drivers

The rating reflects the risk profile of Apna Microfinance Bank ("the bank"). Apna is a small-tier player in Pakistan's microfinance sector with ~2.93% share in the total gross loan portfolio. The Bank has 113 business locations comprising 111 branches and 2 service centers. Overall performance indicators depicted a deteriorated outlook in CY21 amidst an economic slowdown exacerbated by the aftermaths of the global pandemic. Therefore, the repercussions were witnessed in the form of declined markup earned and increasing infection. Further challenges in recovery and markup suspension led to a diminution in interest income. During 9MCY22, the bank witnessed a decline in income from advances to PKR 1.5bln (9MCY21: PKR 2.1bln) whereas, on the investment side, gross markup decreased to PKR 380mln (9MCY21: PKR 513mln). At end-Sep22, the earning assets of the company also decreased to PKR 11.2bln (end-Sep21: PKR 16.9bln) attributable to a sharp decrease in the bank's deposits. Short term-investments reflected improvement and comprise government securities. The infection also enhanced to stand at 26.7% at end-Sep22 reflecting a negative outlook. The equity base of the bank has also reflected a sizeable decline. The outlook on the rating represents the challenges that Bank's business and financial risk profile are facing. These impediments are exhibited in declining profitability, increasing infection, decrease in markup earned, and accumulating losses. The management's commitment to recouping the asset health and consolidating the bank's position within the stipulated time is essential. The bank has announced the initiation of the due diligence process for the merger with another microfinance bank. As per the management, the merger is at an advanced stage (with due diligence completed) and shall be concluded soon. The merger and the due diligence is also announced by the other entity, with which Apna Bank is getting merged. If the merger is realized, the sponsors believe that this will improve their ability to saturate both rural and urban areas with microfinance services and expand our focus on women and rural customers. Further capitalization plans of the merged entity are under consideration. However, Bank's CAR stands still below the regulatory benchmark of 15%.

The ratings are dependent upon the bank's ability to aptly combat the emerging risks under the current scenario in order to improve its business and financial risk profile. The ratings are also kept under "Watch" with the negative outlook incorporating challenges on the profitability front and fulfilling MCR requirements. Compliance with CAR is essential, going forward. Besides, turning loss into profitability is imperative.

Disclosure

Name of Rated Entity	Apna Microfinance Bank Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology | Microfinance Institution Rating(Jun-22),Methodology | Correlation Between Long-term & Short-term Rating Scales(Jun-22),Methodology | Rating Modifiers(Jun-22)
Related Research	Sector Study | Microfinance(Sep-22)
Rating Analysts	Sehar Fatima | sehar.fatima@pacra.com | +92-42-35869504

Profile

Structure Apna Microfinance Bank Limited ("the bank") was incorporated in May 2003 as a Public Limited Company under the Companies Act, 2017 (formerly Companies Ordinance, 1984). The bank is listed on Pakistan Stock Exchange (PSX) since the commencement of its operations in 2005 under the Microfinance Institution Ordinance of 2001.

Background In June-15, the bank was granted a national-level license after completion of regulatory capital requirements. Presently, the bank operates with a network of 111 branches spread across Pakistan.

Operations With its core business purpose of poverty alleviation and financial inclusion, the bank is offering a wide variety of lending products customized according to the needs of various communities. These include loans for farmers, Livestock loans, Agri-loans, House loans, Tractor Loans, Salary loans, and Business loans.

Ownership

Ownership Structure The Bank is a part of the United International Group (UIG) with a major ownership stake of ~46.50% vesting with the United Insurance Company Limited and ~19.34% with the United Track Systems (Private) Limited.

Stability Going forward, ownership of the bank is expected to change as there is a due diligence process going on. The merger and the due diligence are also announced by the other entity, with which Apna Bank is getting merged. If the merger is realized, the sponsors believe that this will improve their ability to saturate both rural and urban areas with microfinance services and expand our focus on women and rural customers. Further capitalization plans of the merged entity are under consideration.

Business Acumen United International Group (UIG) has gradually strengthened its foothold in various business ventures. Currently, the group has interests in microfinance, insurance, tracking business, information technology, agriculture, and business consultancy. UIG is led by its Founder and Chairman – Mian Akram Shahid– the single largest shareholder.

Financial Strength United Insurance and Universal Insurance are the two main Companies of the group. The sponsor's willingness to support the bank is evident from the capital injection by the sponsors historically.

Governance

Board Structure The overall control of the bank vests with nine members. The bank has two independent directors on the Board as per the Prudential Regulations requirement for MFBs. The board has four sub-committees; (i) Audit Committee (ii) HR and Remuneration Committee (iii) Risk and Compliance Committee, and (iv) Monitoring Committee.

Members' Profile Strengthening the governance framework to support operational expansion is important. Mr. Wajahat Malik has been appointed as the CEO and president. All the board members are experienced professionals carrying experience of an average of over ~20 years. Despite other responsibilities, board members remained available for the Bank.

Board Effectiveness During the year, six board meetings were held; the attendance of the board remained strong in the meetings. The board and committee meeting minutes are formally maintained, showing the high attendance of the members.

Transparency The audit committee of the bank comprises five members and is chaired by an independent director, Mr. Abdul Aziz Khan. A separate Internal Audit Department is in place which reports independently to the Audit Committee. RSM Avais Hyder Liaquat Nauman & Co. Chartered Accountants are the external auditors of the Bank. They have expressed an unqualified opinion on the financials for CY21.

Management

Organizational Structure A total of seven department heads report directly to the President. The SAM Department with reporting line to COO has been established as collateral to the disbursements to strengthen the recovery ratio.

Management Team The management positions were filled by qualified professionals to strengthen departmental results. These included the Head of SAM, the Head of Business, and the Head of Product Development.

Effectiveness Six Management Committees are in place namely i) Asset Liability Management (ALCO) ii) Credit, iii) Management, iv) Compliance, v) HR and vi) IT Steering at the senior management level to ensure operational efficiency and efficient decision-making.

MIS To enhance data safety, management has significantly improved the Data collection and management centre and has acquired a program for compliance handling. Instituting a new SAM department has been the most essential ingredient in contributing to restoring effective risk management for the bank.

Risk Management Framework As a consequence of the SBP inspection (as stated above), the bank envisaged betterment in risk management through improvement in the overall control environment by revisiting and devising risk management policies and control procedures to manage its credit risk.

Technology Infrastructure Apna Bank uses Auto-banker III (ABIII) as its core-banking software. Developed by a local vendor, ABIII provides flexibility to consolidate records based on branch, repayment behavior, classification of loan, and borrower profile.

Business Risk

Industry Dynamics Pakistan Microfinance Industry (MFI) comprises 50 microfinance providers including 30 microfinance institutions (MFIs). Active Borrowers continued the increasing trend as 8.5 million borrowers were achieved during CY22, an increase of 5.6% compared to CY21. Similarly, the GLP surpassed PKR 448bln during CY22, an increase of 26.1% compared to the GLP in CY21. The further analysis explains the major contribution to the growth of active borrowers and GLP was contributed by the MFB peer group where Mobilink MFB was at the top of the list due to the significant adoption of digital credit and greater outreach to the customer base. NBMFCs peer group also contributed to the increase by adding 94,000 active borrowers and PKR 2.6bln in GLP. In the case of MFBs, PAR > 30 days slightly increased to 5.3% (CY21: 5.2%). However, the PAR > 30 days of MFIs recovered to report at 4.1% in CY22 (CY21: 5.5%).

Relative Position At end-Sep22, the bank grabbed largely same market share in terms of the gross loan portfolio (CY21: 2.93%).

Revenue The markup earned witnessed a sizable dip (CY21: PKR 908mln; CY20: PKR 3.4bln) attributable to a significant decline in advances recorded at PKR 395mln (CY20: PKR 2.6bln). During 9MCY22, markup earned was recorded at PKR 1.9bln (9MCY21: PKR 2.5bln). The bank's non-markup income was recorded at PKR 117mln (CY20: PKR 177mln).

Profitability During CY21, the bank's non-markup expenses remain unchanged and clocked in at PKR 2bln. The bank booked provisioning of PKR 86mln (CY20: PKR 70mln). The bank's profitability took a major hit and recorded losses of PKR 1.9bln (CY20: PKR 37mln). During 9MCY22, the bank's bottom line recorded losses of PKR 3.3bln.

Sustainability At present, the bank's core focus is on increasing its core profitability and meeting the curtailed capital adequacy ratio (CAR).

Financial Risk

Credit Risk During CY21, the Gross Loan Portfolio (GLP) increased to PKR 11.9bln (end-Dec20: PKR 10bln). The infection ratio also increased to 5.3% (end-Dec20: 4.6%). In end-Sep22, the Gross loan portfolio was recorded at PKR 8.6bln. The infection ratio immensely increased to 26.7%.

Market Risk The short-term investments of the bank declined to PKR 1.1bln (end-Dec20: PKR 1.6bln). The fall consisted of a decline in government securities. At end-Sep22, the short-term investments increased to PKR 1.7bln.

Funding The bank funding is majorly fueled through deposits (end-Dec21: PKR 22bln; end-Dec20: PKR 26.1bln). At end-Sep22, the total deposits of the Bank recorded a slight decrease to PKR 20.8bln.

Cashflows & Coverages The liquidity profile of the bank was diluted at end-Dec21, due to a decrease in the liquid assets-to-deposits ratio to 31.8% (end-Dec20: 51.6%). Also, a decline in investment led to a decrease in liquid assets on an overall basis. At end-Sep22, the liquid assets-to-deposits ratio was recorded at 24.1%.

Capital Adequacy At end-Dec21, the bank's equity base recorded a decline to stand at PKR 442mln (end-Dec20: PKR 2.2bln). At end-Sep22, the bank remained non-compliant in meeting the minimum CAR requirement of 15%.

PKR mln

Apna Microfinance Bank Listed Public Limited	Dec-22 12M	Dec-21 12M	Dec-20 12M	Dec-19 12M
A BALANCE SHEET				
1 Total Finances - net	7,678	11,458	10,118	8,685
2 Investments	1,739	1,160	1,604	946
3 Other Earning Assets	1,819	4,285	9,505	5,464
4 Non-Earning Assets	6,664	6,726	7,502	5,254
5 Non-Performing Finances-net	1,087	148	101	194
Total Assets	18,986	23,777	28,831	20,543
6 Deposits	20,824	22,084	26,179	18,317
7 Borrowings	-	0	3	7
8 Other Liabilities (Non-Interest Bearing)	1,026	1,250	390	345
Total Liabilities	21,851	23,334	26,572	18,669
Equity	(2,865)	442	2,259	1,872
B INCOME STATEMENT				
1 Mark Up Earned	1,959	908	3,418	2,900
2 Mark Up Expensed	(1,169)	(1,459)	(1,389)	(1,209)
3 Non Mark Up Income	117	162	177	490
Total Income	907	(388)	2,206	2,181
4 Non-Mark Up Expenses	(1,646)	(2,169)	(2,078)	(1,798)
5 Provisions/Write offs/Reversals	(2,950)	(86)	(70)	(294)
Pre-Tax Profit	(3,689)	(2,643)	58	89
6 Taxes	382	712	(21)	(36)
Profit After Tax	(3,307)	(1,931)	37	54
C RATIO ANALYSIS				
1 Performance				
Net Mark Up Income / Avg. Assets	3.7%	-2.1%	8.2%	8.9%
Non-Mark Up Expenses / Total Income	181.5%	-558.5%	94.2%	82.4%
ROE	136.5%	-143.0%	1.8%	3.2%
2 Capital Adequacy				
Equity / Total Assets (D+E+F)	-15.1%	1.9%	7.8%	9.1%
Capital Adequacy Ratio	N/A	11.8%	11.8%	11.7%
3 Funding & Liquidity				
Liquid Assets / (Deposits + Borrowings Net of Repo)	24.1%	31.8%	51.6%	42.3%
(Advances + Net Non-Performing Advances) / Deposits	41.6%	52.1%	38.7%	47.9%
Demand Deposits / Deposits	52.5%	46.7%	51.3%	56.6%
SA Deposits / Deposits	47.5%	53.3%	48.7%	43.4%
4 Credit Risk				
Non-Performing Advances / Gross Advances	36.1%	5.3%	4.6%	5.4%
Non-Performing Finances-net / Equity	-37.9%	33.4%	4.5%	10.4%

Corporate Rating Criteria

Scale

Credit Rating

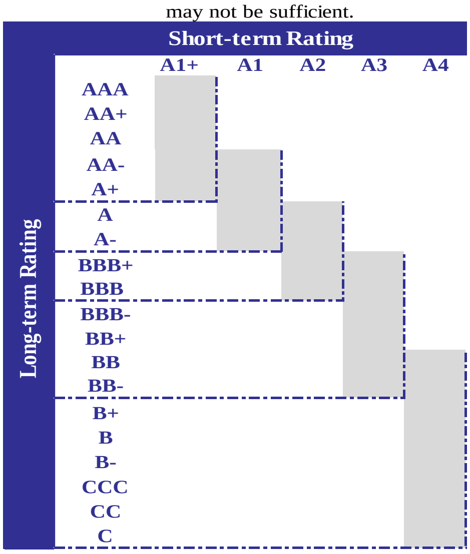
Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

Long-term Rating

Scale	Definition
AAA	**Highest credit quality.** Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments
AA+ AA AA-	**Very high credit quality.** Very low expectation of credit risk. Indicate very strong capacity for timely payment of financial commitments. This capacity is not significantly vulnerable to foreseeable events.
A+ A A-	**High credit quality.** Low expectation of credit risk. 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.
BBB+ BBB BBB-	**Good credit quality.** Currently a low expectation of credit risk. 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.
BB+ BB BB-	**Moderate risk.** Possibility of credit risk developing. 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+ B B-	**High credit risk.** 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.
CCC CC C	**Very high credit risk.** Substantial credit risk “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.
D	Obligations are currently in default.

Short-term Rating

Scale	Definition
A1+	The highest capacity for timely repayment.
A1	A strong capacity for timely repayment.
A2	A satisfactory capacity for timely repayment. This may be susceptible to adverse changes in business, economic, or financial conditions.
A3	An adequate capacity for timely repayment. Such capacity is susceptible to adverse changes in business, economic, or financial
A4	The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions. Liquidity may not be sufficient.



**The correlation shown is indicative and, in certain cases, may not hold.*

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 some material identifiable event with indeterminable rating implications. 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 rating 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.

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

Harmonization A change in rating due to revision in applicable methodology or underlying scale.

Surveillance. Surveillance on a publicly disseminated rating opinion is carried out on an ongoing basis till it is formally suspended or withdrawn. A comprehensive surveillance of rating opinion is carried out at least once every six months. However, a rating opinion may be reviewed in the intervening period if it is necessitated by any material happening.

Note. This scale is applicable to the following methodology(s):

a) Broker Entity Rating
b) Corporate Rating
c) Debt Instrument Rating
d) Financial Institution Rating
e) Holding Company Rating
f) Independent Power Producer Rating
g) Microfinance Institution Rating
h) Non-Banking Finance Companies Rating

Regulatory and Supplementary Disclosure
(Credit Rating Companies Regulations,2016)

Rating Team Statements
(1) Rating is just an opinion about the creditworthiness of the entity and does not constitute recommendation to buy, hold or sell any security of the entity rated or to buy, hold or sell the security rated, as the case may be | Chapter III; 14-3-(x)

2) **Conflict of Interest**
i. The Rating Team or any of their family members have no interest in this rating | Chapter III; 12-2-(j)
ii. PACRA, the analysts involved in the rating process and members of its rating committee, and their family members, do not have any conflict of interest relating to the rating done by them | Chapter III; 12-2-(e) & (k)
iii. The analyst is not a substantial shareholder of the customer being rated by PACRA [Annexure F; d-(ii)] Explanation: for the purpose of above clause, the term “family members” shall include only those family members who are dependent on the analyst and members of the rating committee

Restrictions
(3) No director, officer or employee of PACRA communicates the information, acquired by him for use for rating purposes, to any other person except where required under law to do so. | Chapter III; 10-(5)
(4) PACRA does not disclose or discuss with outside parties or make improper use of the non-public information which has come to its knowledge during business relationship with the customer | Chapter III; 10-7-(d)
(5) PACRA does not make proposals or recommendations regarding the activities of rated entities that could impact a credit rating of entity subject to rating | Chapter III; 10-7-(k)

Conduct of Business
(6) PACRA fulfills its obligations in a fair, efficient, transparent and ethical manner and renders high standards of services in performing its functions and obligations; | Chapter III; 11-A-(a)
(7) PACRA uses due care in preparation of this Rating Report. Our information has been obtained from sources we consider to be reliable but its accuracy or completeness is not guaranteed. PACRA does not, in every instance, independently verifies or validates information received in the rating process or in preparing this Rating Report | Clause 11-(A)(p).
(8) PACRA prohibits its employees and analysts from soliciting money, gifts or favors from anyone with whom PACRA conducts business | Chapter III; 11-A-(q)
(9) PACRA ensures before commencement of the rating process that an analyst or employee has not had a recent employment or other significant business or personal relationship with the rated entity that may cause or may be perceived as causing a conflict of interest; | Chapter III; 11-A-(r)
(10) PACRA maintains principal of integrity in seeking rating business | Chapter III; 11-A-(u)
(11) PACRA promptly investigates, in the event of a misconduct or a breach of the policies, procedures and controls, and takes appropriate steps to rectify any weaknesses to prevent any recurrence along with suitable punitive action against the responsible employee(s) | Chapter III; 11-B-(m)

Independence & Conflict of interest
(12) PACRA receives compensation from the entity being rated or any third party for the rating services it offers. The receipt of this compensation has no influence on PACRA´s opinions or other analytical processes. In all instances, PACRA is committed to preserving the objectivity, integrity and independence of its ratings. Our relationship is governed by two distinct mandates i) rating mandate - signed with the entity being rated or issuer of the debt instrument, and fee mandate - signed with the payer, which can be different from the entity
(13) PACRA does not provide consultancy/advisory services or other services to any of its customers or to any of its customers’ associated companies and associated undertakings that is being rated or has been rated by it during the preceding three years unless it has adequate mechanism in place ensuring that provision of such services does not lead to a conflict of interest situation with its rating activities; | Chapter III; 12-2-(d)
(14) PACRA discloses that no shareholder directly or indirectly holding 10% or more of the share capital of PACRA also holds directly or indirectly 10% or more of the share capital of the entity which is subject to rating or the entity which issued the instrument subject to rating by PACRA; | Reference Chapter III; 12-2-(f)
(15) PACRA ensures that the rating assigned to an entity or instrument is not be affected by the existence of a business relationship between PACRA and the entity or any other party, or the non-existence of such a relationship | Chapter III; 12-2-(i)
(16) PACRA ensures that the analysts or any of their family members shall not buy or sell or engage in any transaction in any security which falls in the analyst’s area of primary analytical responsibility. This clause shall, however, not be applicable on investment in securities through collective investment schemes. | Chapter III; 12-2-(l)
(17) PACRA has established policies and procedure governing investments and trading in securities by its employees and for monitoring the same to prevent insider trading, market manipulation or any other market abuse | Chapter III; 11-B-(g)

Monitoring and review
(18) PACRA monitors all the outstanding ratings continuously and any potential change therein due to any event associated with the issuer, the security arrangement, the industry etc., is disseminated to the market, immediately and in effective manner, after appropriate consultation with the entity/issuer; | Chapter III | 18-(a)
(19) PACRA reviews all the outstanding ratings on semi-annual basis or as and when required by any creditor or upon the occurrence of such an event which requires to do so; | Chapter III | 18-(b)
(20) PACRA initiates immediate review of the outstanding rating upon becoming aware of any information that may reasonably be expected to result in downgrading of the rating; | Chapter III | 18-(c)
(21) PACRA engages with the issuer and the debt securities trustee, to remain updated on all information pertaining to the rating of the entity/instrument; | Chapter III | 18-(d)
Probability of Default
(22) PACRA´s Rating Scale reflects the expectation of credit risk. The highest rating has the lowest relative likelihood of default (i.e, probability). PACRA´s transition studies capture the historical performance behavior of a specific rating notch. Transition behavior of the assigned rating can be obtained from PACRA´s Transition Study available at our website. (www.pacra.com). However, actual transition of rating may not follow the pattern observed in the past | Chapter III | 14-(f-VII)
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