The Pakistan Credit Rating Agency Limited

Rating Report

Pak-Libya Holding Company (Pvt.) Limited

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
27-Dec-2018	AA-	A1+	Negative	Maintain	-
14-Jun-2018	AA-	A1+	Negative	Maintain	-
18-Dec-2017	AA-	A1+	Negative	Maintain	-
23-Jun-2017	AA-	A1+	Negative	Maintain	-
25-Jun-2016	AA-	A1+	Negative	Maintain	-

Rating Rationale and Key Rating Drivers

Development Financial institutions (DFIs) largely operate on turf common to commercial banks. Limited depth in participation towards development of long gestation projects, low funding base, and high competition becomes their key challenges. Joint Venture Financial Institutions are DFIs jointly established by the two sovereigns with primary objective of identifying and nurturing multiple development initiatives. Their ratings are mainly characterized by sovereign ownership, adequate standards of governance, and relatively conservative risk appetite.

The ratings of Pak Libya reflect organic growth of the company and minimum capital requirement gap gradually being abridged. Benefiting from the increasing credit off take in the country, lending side of Pak Libya picked up pace along with sustaining the quality. Treasury operations continue to strengthen the financial position of the company. Investment in government securities dominates the book with limited exposure in equity market through investments in diversified blue chip stocks. However, with significant increase in cost structure especially interest expense, Company booked an operating loss in 9MCY18. The management continues to cautiously expand its existing loan book through corporate finance activities and further penetrating in SME segment. The management expects to capitalize on new avenues led by economic activities.

Last year, a Special Purpose Vehicle named Kamoke Powergen (Pvt.) Limited (KPL) was incorporated, to apply for power generation license from NEPRA so as to increase viability of KEL – Pak Libya's largest nonperforming exposure – a strategic investment on the books. However, the exposure was completely provided for. Although the management is trying to pursue it, owing to non-viability of RFO plants in a current energy industry dynamics, the sale of plant seems challenging. Company's sovereign parentage have not translated fully in meeting its regulatory capital requirement deficiency as of date. The approval for further extension in compliance with capital requirement remains dependent upon commitment from sponsoring Governments.

The ratings have a "negative outlook", signifying the need to comply with regulatory minimum capital requirement (shortfall of PKR 1.6bln as at end-Dec'17 and PKR 1.7bln as at end-Sep'18). Consistent efforts by the management to stabilize revenue stream and add further diversity to operations would remain critical. Meanwhile, sustaining asset quality would help maintain the ratings. Timely sell-off of KEL is important for the ratings.

Disclosure

Name of Rated Entity	Pak-Libya Holding Company (Pvt.) Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology | Financial Institution(Jun-18),Methodology | Criteria | Rating Modifier(Jun-18),Methodology | Correlation Between Long-Term And Short-Term Rating Scale(Jun-18)
Related Research	Sector Study | DFI(Jun-18)
Rating Analysts	Sehar Fatima | sehar.fatima@pacra.com | +92-42-35869504

Profile

Structure Pak Libya Holding Company (Pvt.) Limited was incorporated in Pakistan as private limited company on October 14, 1978 with the registered office in Karachi. The tenure of the company has increased by two government's up to October 14, 2038.

Background Pak Libya is a Joint Venture Financial Institute (JVFI), operating within the framework of commercial and banking laws of Pakistan. Pak Libya is equally owned by the Government of Islamic Republic of Pakistan (GoP), represented through SBP, and the Government of Libya, represented through Libyan Foreign Investment Company (LAFICO), implying strong sovereign support.

Operations The primary objective of Pak Libya is to promote development of industrial and economic infrastructure of the country, by supporting both industrial and service sectors. Pak Libya's three core avenues for asset building are loans/leases, capital and money market operations, and project financing for infrastructure development. Company's non-fund based activities include syndication of local/foreign currency transactions, issuance of guarantees, underwriting, corporate finance advisory services, and letter of credit facilities.

Ownership

Ownership Structure Pak Libya Holding Company (Pvt.) Limited is an equally owned joint venture between Pakistan and Libya. State Bank of Pakistan (SBP) represents Government of Pakistan, while Libyan Foreign Investment Company (LAFICO) represents the Government of Libya.

Stability The company's ownership structure is expected to remain same in foreseeable future.

Business Acumen The business acumen of sponsors is considered adequate.

Financial Strength The ability to support the company in case of financial need is considered strong however, willingness to support may vary in different situations.

Governance

Board Structure The overall control of the company vests with six-member board of directors including the MD/CEO, DMD and four nonexecutive directors having equal representation from both governments. Board's Chairman is the representative of Government of Libya, while Company's Managing Director is representing Government of Pakistan.

Members' Profile All the board members carry vast experience from diversified sectors. The Chairman of the board, Mr. Bashir B. Omer, a representative of Government of Libya, has worked as an investment banker and has over 20 years of experience. All the directors are professionally trained, adding effectiveness to the board. The board members carry financial industry experience with most of them handling investment portfolio in past.

Board Effectiveness The board has formulated four board committees for effective monitoring. All board members attended five board meetings conducted during the year except for Mr. Fazal Ur Rehman who attended only four meetings. Minutes made were detailed and well captured.

Financial Transparency Board has set-up a three member Audit Committee that reports to the Board. M/s Grant Thornton Anjum Rahman, Chartered Accountants, are external auditors of the Company and have emphasized on matter (KEL and MCR) in their audit report for the year ended December 31, 2017.

Management

Organizational Structure Well-defined organizational set-up of the company falls under the purview of the Managing Director except for Internal Audit; who reports to the Board Audit Committee.

Management Team All the team members carry vast experience in related field. Company's MD/CEO, Mr. Abid Aziz carries financial sector experience of above 30 years. Prior to joining Pak Libya as CEO/MD, he has worked at senior positions within the organization and also has international exposure. Mr. Khaled Joma Ezarzor, Pak Libya's DMD, has previously worked in the company as S.V.P and is associated with LAFICO since long. He has represented LAFICO in China and has an experience of 20 years and above.

Effectiveness The management has multiple committees naming: Credit Committee, Asset and Liability Committee, Risk Management Committee, IT Steering Committee. All these committees include Heads of various divisions. Their primary function is to ensure the implementation of the company's vision and smooth facilitation of operations.

MIS MIS reports used by the head of departments are generated from a combination of systems with some manual reports are also prepared.

Risk Management Framework Cognizant of the risk associated with operations, Pak Libya has installed and implemented various models and manuals to minimize the company wide risks.

Business Risk

Industry Dynamics DFI industry has grown with achieving a CAGR of 11% in the lending portfolio and 10% in funding, over a span of 5 years. Portfolio quality is improving with better risk monitoring and conservative lending. Going forward, to compete with the other financial institutions (commercial banks primarily), the industry players need to identify new niche for the expansion of DFIs operations.

Relative Position Marked 6% share in the lending portfolio of JVFI industry, while it has been able to tap 12% of the JVFI industry's funding base.

Revenues Company's NIMR increased by 20% YOY in 9MCY18 (9MCY18: PKR 240mln; 9MCY17: 202mln), driven by increase in lending portfolio.

Performance Other operating income of the company declined to PKR 65mln in 9MCY18 (CY17: PKR 318mln; 9MCY17: PKR 281mln) backed by decline in gain on sale of investment. Owing to sizable decrease in other operating income, the company's cost to total net revenue witnessed sharp increase to 112% (CY17: 77%), although company's expenses were kept under check. On account of aforementioned factors, the company recorded net loss of PKR 97mln.

Sustainability Going forward, sale of repossessed assets of KEL is management's priority. However, given the current dynamics of power sector the sale of KEL will be a challenge for the company. Pak Libya's management is continuously approaching sponsors to inject equity to bridge the gap required to meet MCR. Management is exploring financial guarantees as revenue stream.

Financial Risk

Credit Risk During 9MCY18, Company was able to maintain its asset book with slight growth of 1%, backed by significant increase in loan given to financial institutions. Advances portfolio was actively managed (28% incline in total finances). In CY17, top three sector exposure are Power (19%), Textile (15%) and Chemical and Pharmaceuticals (14%). Asset quality witnessed slight improvement as impaired stood at 35% of Gross advances in 9MCY18 (CY17: 39%) from which 78% of provision was kept for loan losses in 9MCY18 as well as CY17.

Market Risk During 9MCY18, investment in Govt. securities increased by 27% which comparises 92% of the total investment portfolio. Within the government securities PIBs and T-Bills have weightage of 94% and 6% respectively as at end-Sep18. The top sectors for equity investments remained Fertilizer, Banks and Insurance. Pak Libya made a strategic exposure in Kamoki Energy Limited (KEL) through preference shares of PKR 300mln and ordinary shares of PKR 405mln. It's a 70 MW Rental Power Plant (RPP) and a joint venture between Pak Libya and Tapal family. In CY17, a Special Purpose Vehicle named Kamoke Powergen (Pvt.) Limited (KPL) was incorporated, to apply for power generation license from NEPRA so as to increase KEL's prospects of sale.

Liquidity And Funding Assets and Liabilities Committee is responsible for supervising interest rate risks and maturity mismatch management. Liquid assets have improved as percentage of deposits and borrowings (9MCY18: ~70%; CY17: 57%), which provide a comfortable cushion to borrowings and deposits. The company's deposit base witnessed significant expansion to stand at PKR 1.0bln (CY17: PKR 39mln). Company's borrowings which consist of Repo Borrowing of PKR 7,350mln (CY17: PKR 5,368mln) and remaining other borrowings from financial institutions.

Capitalization Equity base (9MCY18: PKR 4.6bln CY17: PKR 4.7bln), mainly comprising Tier-I capital remains below the MCR level. Thus does not absorb the impact of any adverse macroeconomic performance related shocks. SBP has granted extension for compliance till June'18. Pak Libya's capital adequacy stands at 22.8% (CY17: 31.5%).

Pak Libya Holding Company (Pvt.) Limited

(PKR mln)

BALANCE SHEET	30-Sep-18	31-Dec-17	31-Dec-16	31-Dec-15
	9M	Annual	Annual	Annual
Assets				
Earning Assets				
Advances	3,064	2,943	2,509	2,334
Lease	626	213	209	247
Debt Instruments	2,859	2,244	1,382	1,336
- Total Finances	**6,549**	**5,400**	**4,100**	**3,918**
Govt Securities	8,391	6,616	10,891	8,623
Equity Investments	768	1,246	1,303	1,340
Investments in Associates & Subsidiaries	5	(405)	(405)	(405)
Mutual Funds	-	-	-	-
- Total Investments	**9,164**	**7,457**	**11,789**	**9,558**
Others	1,176	4,053	1,013	349
Non Earning Assets				
Non Earning Cash	26	59	30	67
Deferred Tax	91	85	26	194
Net Non Performing Finances	448	437	132	684
Fixed Assets & Others	1,862	1,672	1,805	504
Total Assets	**19,317**	**19,163**	**18,895**	**15,274**
Liabilities				
Certificates of Investment	1,070	39	463	1,737
Borrowings	13,611	14,367	13,392	9,441
Interest Bearing Liabilities	**14,681**	**14,406**	**13,855**	**11,178**
Non Interest Bearing Liabilities	**260**	**202**	**279**	**201**
Equity				
Total Equity	4,616	4,713	4,669	3,874
Revaluation Surplus	(240)	(158)	92	21
TOTAL LIABILITIES & EQUITY	**19,317**	**19,163**	**18,895**	**15,274**
INCOME STATEMENT				
Interest/ markup earned	1,081	1,017	1,179	1,386
Interest/ markup expensed	(841)	(752)	(866)	(1,026)
Net Interest/ markup revenue	**240**	**265**	**313**	**360**
Other Income	65	318	119	444
Total revenue	**304**	**583**	**433**	**804**
Non Interest/ Non Markup expensed	(343)	(450)	(443)	(392)
Pre-provision Profit	(39)	133	(10)	412
(Provision)/ Reversal	(7)	(49)	1,042	61
Taxes	(52)	(36)	(241)	(167)
Net Income	**(97)**	**48**	**791**	**305**
Ratio Analysis				
Performance				
ROE*	-2.8%	1.0%	18.5%	8.2%
Cost-to-Total Net Revenue	112.7%	77.2%	102.4%	48.8%
Capital Adequacy				
Equity / Total Assets	23.9%	24.6%	24.7%	25.4%
Capital Adequacy ratio as per SBP	22.8%	31.5%	36.6%	38.4%
Funding & Liquidity				
Liquid Assets/ Deposits & Borrowings	69.7%	57.1%	92.1%	93.4%
Finances/ Deposits & Borrowings	47.7%	40.5%	30.5%	40.9%
Loan Loss Coverage				
Loan Loss Provisions/ NPLs	77.6%	77.9%	92.7%	79.6%
Net Impaired Lending/Total Equity	9.7%	9.3%	2.6%	16.9%

**** Annualized***

Rating Scale

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.

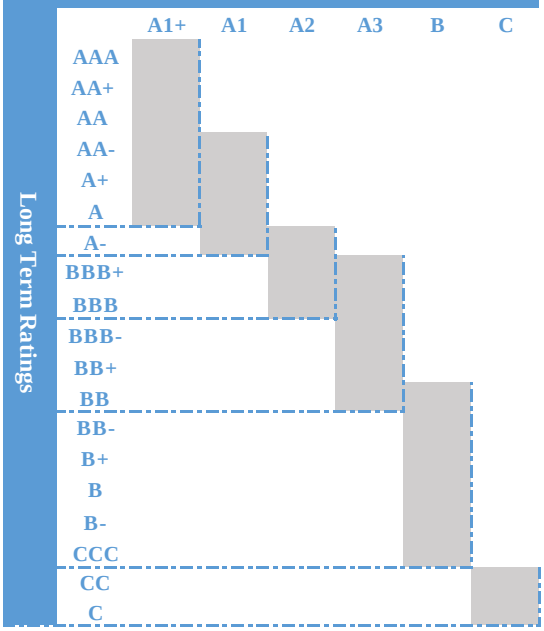
Long Term Ratings

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 Ratings

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 conditions.
B	The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions.
C	An inadequate capacity to ensure timely repayment.

Short Term Ratings



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.

Withdrawn 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 surveill the opinion due to lack of requisite information.

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

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.
(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)
Proprietary Information