RATING REPORT

Pak Brunei Investment Company Limited (PBICL)

REPORT DATE:
June 28, 2024

RATING ANALYSTS:

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RATING DETAILS				
Rating Category	Latest Rating		Previous Rating	
	Long-term	Short-term	Long-term	Short-term
Entity	AA+	A-1+	AA+	A-1+
Rating Outlook	Stable		Stable	
Rating Action	*Reaffirmed*		*Reaffirmed*	
Rating Date	*June 28, '24*		*June 27, '23*	

COMPANY INFORMATION	
Incorporated in 2006	**External Auditors:** M/s Yousuf Adil Chartered Accountants
Unlisted Public Company	**Chairperson of the Board**: Ms. Dk Noorul Hayati Pg Julaihi
Key Shareholders (with stake 5% or more):	**CEO & Managing Director**: Mr. S. M. Aamir Shamim
Brunei Investment Agency – 50.0%	
Ministry of Finance, Government of Pakistan – 49.999%	

APPLICABLE METHODOLOGY(IES)

VIS Entity Rating Criteria:
Government Supported Entities
https://docs.vis.com.pk/docs/Meth-GSEs202007.pdf
Financial Institutions Rating Methodology
https://docs.vis.com.pk/Methodologies%202024/Financial-Institution-v2.pdf

APPLICABLE RATING SCALE(S)

Rating Scales & Definitions:
https://docs.vis.com.pk/docs/VISRatingScales.pdf

Pak Brunei Investment Company Limited

OVERVIEW OF THE INSTITUTION

PBICL was incorporated as a Development Finance Institution (DFI) in 2006 and operates as a joint venture of (Government of Pakistan and Brunei Investment Agency (BIA). In 2023, Yousuf Adil Chartered Accountants conducted the external audit of financial statements. The audit firm is listed in the 'A' category of SBP's panel of auditors.

Profile of Chairperson

Ms. Noorul is a Portfolio Manager in the Absolute Return Strategy in BIA, the Sovereign Wealth Fund of the GoB. Ms. Noorul has been associated with BIA for 18 years. Her previous roles included Assistant Portfolio Manager and Analyst for Macro and Fixed Income Group. She has also managed the European Fixed Income Portfolio. Before moving onto current role, she was co-leading the private equity team. In her current role she is leading a team of professionals focused on hedge fund investments across the globe. She has also previously served as Director in Audley Insurance Company, wholly owned by BIA. She holds a degree with a major in Economics from Universiti Brunei Darussalam.

Profile of CEO & Managing Director:

Mr. S. M. Aamir Shamim has served as Group Head of Treasury and Financial Institutions at BankIslami Pakistan Limited (BIPL). He has also served as SEVP Finance & Treasury Group at the Islamic Bank of Thailand.

RATING RATIONALE

Pak Brunei Investment Company Limited (PBICL) is a Development Finance Institution (DFI) that provides financial assistance to industrial and agricultural projects. Regulated by the State Bank of Pakistan (SBP), PBICL operates through its head office in Karachi and a branch office in Lahore. It is a joint venture equally owned by the Government of Pakistan (GoP) and the Government of Brunei (GoB). The GoP's interests are represented by the Ministry of Finance (MoF), while the GoB's interests are represented by the Brunei Investment Agency (BIA). It is headed by Mr. S. M. Aamir Shamim as CEO & Managing Director, who was appointed in May 2023.

The Board of directors comprises of four directors, two nominated by Government of Brunei and two by Government of Pakistan. The Board is headed by Ms. Dk Noorul Hayati Pg Julaihi.

Sector Update

The financial sector in Pakistan has been navigating a challenging macroeconomic landscape. Despite facing headwinds such as high inflation, elevated interest rates, and geopolitical uncertainties, the sector has demonstrated resilience and adaptability in supporting economic stability. One of the important factors contributing to the sector's resilience has been its strong capitalization and liquidity. Banks and Development Financial Institutions (DFIs) in Pakistan remain well-capitalized. This ensures that they are equipped to absorb potential shocks and maintain financial stability. DFIs continued to face the challenge of lack of cheap sources of funding. Given limited good credit available in the market for deployment in a heightened credit risk environment, spreads remained under pressure. Consequently, investment portfolios were built up through leveraging the balance sheet for profitability uptick on volume growth.

The government's successful negotiation of the IMF's Stand-By Arrangement (SBA) program, culminating in a Staff-Level Agreement and disbursement of funds, has provided additional support to market confidence and exchange rate stability, with positive implications for the banking sector. In terms of monetary policy dynamics, the State Bank of Pakistan (SBP) has maintained a cautious stance, balancing the imperative of containing inflationary pressures while supporting economic growth. Even as headline inflation has moderated from peak levels, it remains elevated, prompting the SBP to retain the policy rate in the first half of 2024 and only reducing it by 1.5% in June 2024. This delayed rate cut reflects central bank's commitment to anchoring inflation expectations and safeguarding macroeconomic stability. We expect policy rate to reduce by another 1-1.5% by the end of 2024.

Looking ahead, the financial sector faces both challenges and opportunities. Continued vigilance in managing credit quality and liquidity risks will be vital, especially amidst evolving macroeconomic dynamics and policy uncertainties. Moreover, the sector's role in supporting the government's reform agenda, particularly in areas such as taxation, energy, and privatization of state-owned enterprises, will be critical in fostering sustainable economic growth and financial stability.

Advances: Amid socio-political and economic challenges, including rising inflation and high interest rates, PBICL adopted a cautious strategy. Consequently, the gross advances portfolio declined from Rs. 24.7 billion in CY22 to Rs. 20.7 billion in CY23. The advances portfolio remained concentrated in textiles (19%), chemicals and pharmaceuticals (17%), food and beverages (13%), and power (12%). The portfolio is vested in the private sector, with a significant corporate segment. Efforts to enhance the SME segment increased its contribution from 9% to 11%. PBICL plans to expand its advances book by around 20%, targeting health, power, and export-based textiles.

Asset Quality: Credit risk from the advances book is considered moderate, with no significant write-offs and about 72% of the portfolio having an Obligor risk rating of '3'. Compared to peers, the asset quality indicators are favorable. Management is emphasizing recoveries and is actively working to expedite the realization of forced sale assets.

Asset quality deteriorated to some extent in CY23, with gross infection rates rising to 5.4% by December 2023 and further to 6.2% in Q1 CY24. This was due to a marginal increase in non-performing loans, particularly in the power and steel sectors, and a decrease in the overall portfolio size. In response, the Company raised its provisioning charge by Rs. 549 million in CY23, improving provisioning coverage from 57% to 93% and reducing net infection to 0.8%. However, the additions to non-performing loans in Q1 CY24 were only partially covered, causing net infection to rise slightly to 1% by the end of Q1 CY24. Having said that, there have also been some encouraging signs towards recovery such as towards the end of Q1FY24, the Company was able to get last injunction order vacated on couple of its Non-Banking Assets (NBAs). These NBAs were related to a non-performing loan. As a result, the Company was able to secure its possession. The property is under sale process. More importantly, during Q2CY24, the Company succeeded to execute settlement of one of its long outstanding non-performing loans. On June 13, 2024, the Honorable Court has also endorsed the said settlement. Further, during Q1CY24, the Company also succeeded in completion of the auction process of another non-performing loan. The process is at its advance stage of validation from the court.

Investments: Amid challenging economic conditions and higher benchmark rates set by the SBP, the Company leveraged higher yields on government securities to optimize its balance sheet. By participating in SBP's open market operations (OMO), the Company's net investment portfolio saw substantial growth, mainly in government securities, increasing by about four times by the end of December 2023 and Q1 2024. This growth was primarily in floating rate PIBs, which made up 93% of the total government securities investments by the end of March 2024. The Company's exposure to equities was minimal, at 0.94% of total investments, focusing majorly on power stocks. Non-government debt securities, mainly TFC and Sukuk holdings of banks, accounted for 1.4% of the total investment portfolio.

Credit risk from the investment portfolio remains low due to the majority of investments being in government securities. However, market risk exposure is high. By March 2024, the total deficit on the government securities portfolio increased to Rs. 2.4 billion (from Rs. 1.8 billion in December 2023) due to increase in mark to market losses on floating rate PIBs from a surplus of Rs. 31.5 million in December 2023 to a deficit of Rs. 758.4 million in March 2024. Mark-to-market losses on fixed rate PIBs, which make up about 4% of the total government securities holdings, were significant at Rs. 1.7 billion but reduced from Rs. 1.8 billion when compared with Dec 23. The average duration of the floating rate portfolio is less than three years, and less than five years for the fixed rate portfolio. It is expected that with falling interest rates, mark-to-market losses will start declining for the fixed rate portfolio.

The aggressive increase in the investment portfolio through repo borrowings led to a leverage ratio of 3.4%, leaving limited room for further expansion given the SBP's requirement of 3%. Moving forward, management plans to reduce government securities exposure and increase their equities portfolio, focusing on dividend-yielding stocks.

Liquidity: The liquidity profile of DFI is strengthened by the availability of funding lines and adequate coverage of deposits and borrowings through liquid assets, which improved significantly to 55.2% by the end of March 2024 (from 39.1% in CY23 and 26.4% in CY22), driven by growth in the investment portfolio. Due to the high cost of corporate deposits, the Company does not rely on deposits other than when cash margins are required from customers, consequently the nominal deposits of Rs. 54.8 million reported in 2022 were reduced to zero by year-end and the first quarter end.

The Company funded investments in long-term government securities with shorter-tenure borrowings, creating a liquidity gap of Rs. 130 billion up to 1 month and Rs. 17 billion in the 3-6 months bucket.

However, this risk is manageable as funding can be arranged against securities through OMO or SBP discounting.

Although DFIs are not required to maintain a Liquidity Coverage Ratio (LCR), the Company's LCR declined to 94% by the end of March 2024 due to a higher proportion of unsecured borrowings compared to the previous year. The Net Stable Funding Ratio (NSFR) remained well above 100% during the review period.

Profitability: Higher benchmark rates resulted in higher yields on earning assets, which rose to 19.31% in CY23, but also increased the cost of funding to 19.11%, leading to a lower spread of 0.2%. Despite the reduced spread, the expanded earning asset base in 2023 boosted net mark-up income, with investment income contributing 83% to the total mark-up income. Non-markup income surged by 93% in CY23, driven mainly by higher dividend income and gains on the sale of securities, while fee and commission income grew modestly by 9%. Furthermore, despite higher provisioning expense, increased mark-up incomes led to a post-tax profit of Rs. 847 million, up 69% from the previous year.

Profitability in Q1 CY24 was pressured by spread compression. Yields in the secondary market fell below the policy rate since November 2023, anticipating a rate cut. Consequently, asset yields declined while the cost of funds remained flat, reducing net interest income in Q1 CY24. With expected interest rate cuts, repricing of liabilities will likely affect profitability until the end of the second quarter, but capital gains from the investment portfolio are expected to support the bottom-line profitability. Efficiency ratio has shown an improving trend and remains favorable compared to peers.

Capitalization: The capitalization profile of PBIC remained strong despite the impact of IFRS 9. Tier-1 capital improved due to surpluses from the revaluation of investments. This, along with a decrease in risk-weighted assets (RWAs) primarily from lower credit risk assets, led to an increase in the capital adequacy ratio (CAR) to 26% as of December 2023. Net NPLs to tier-1 capital decreased to 1.3% from 5.0% in December 2022, reflecting improved coverage. However, by March 2024, the CAR declined to 22% due to decline in eligible capital majorly on account of increase in unrealized losses. Despite this decline, overall capitalization indicators remain robust, with CAR well above regulatory requirements. PBIC has paid out Rs. 300 million dividends for the year ended December 31, 2023. Currently, PBICL's CAR aligns with peers and meets benchmarks for assigned ratings.

Pak Brunei Investment Company Limited — Appendix I

FINANCIAL SUMMARY	*Amount in PKR Billions*				
BALANCE SHEET	**2020**	**2021**	**2022**	**2023**	**Q1'24**
Net Investments	17,482.9	26,246.6	44,805.4	158,671.1	189,674.0
Net Advances	19,133.9	20,300.1	24,207.9	19,609.9	17,634.5
Total Assets	40,253.4	51,449.8	79,937.6	188,070.7	222,333.4
Borrowings	27,763.4	40,284.8	68,320.2	174,594.0	207,768.5
Deposits & other accounts	830.0	50.0	54.8	-	-
Paid-Up Capital	6,000.0	6,000.0	6,000.0	6,000.0	6,000.0
Tier-1 Equity	8,046.7	8,435.7	7,555.7	8,225.1	7,014.7
Net Worth	10,732.6	10,232.0	10,003.2	10,838.9	10,557.6
INCOME STATEMENT	**2020**	**2021**	**2022**	**2023**	**Q1'24**
Net Mark-up Income	767.7	866.2	789.4	1,370.2	185.1
Net Provisioning / (Reversal)	34.0	70.7	(35.3)	237.6	13.2
Non-Markup Income	687.7	340.3	353.2	682.9	189.4
Administrative Expenses	366.2	408.9	420.1	581.2	161.2
Profit (Loss) Before Tax	1,033.4	703.6	743.7	1,209.6	196.2
Profit (Loss) After Tax	718.4	481.3	502.9	847.4	139.3
RATIO ANALYSIS	**2020**	**2021**	**2022**	**2023**	**Q1'24**
Gross Infection (%)	5.03%	4.89%	3.57%	5.44%	6.23%
Provisioning Coverage (%)	43.04%	53.69%	56.78%	86.35%	85.42%
Net Infection (%)	2.93%	2.56%	1.57%	0.78%	0.96%
Net NPLs to Tier-1 Capital (%)	6.96%	6.15%	5.04%	1.87%	2.42%
Capital Adequacy Ratio (C.A.R (%))	26.64%	29.42%	23.02%	26.58%	22.27%
Efficiency (%)	36.66%	37.92%	35.53%	31.74%	51.12%
ROAA (%)	1.47%	1.05%	0.98%	0.76%	0.07%
ROAE (%)	6.58%	4.29%	4.41%	7.32%	1.22%

REGULATORY DISCLOSURES Appendix II

Name of Rated Entity	Pak Brunei Investment Company Limited (PBICL)
Sector	Development Finance Institution (DFI)
Type of Relationship	Solicited
Purpose of Rating	Entity Rating
Instrument Structure	N/A
Statement by the Rating Team	VIS, the analysts involved in the rating process and members of its rating committee do not have any conflict of interest relating to the credit rating(s) mentioned herein. This rating is an opinion on credit quality only and is not a recommendation to buy or sell any securities.
Probability of Default	VIS' ratings opinions express ordinal ranking of risk, from strongest to weakest, within a universe of credit risk. Ratings are not intended as guarantees of credit quality or as exact measures of the probability that a particular issuer or particular debt issue will default.
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Rating History

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
RATING TYPE: ENTITY				
28-June-24	AA+	A-1+	Stable	Reaffirmed
27-Jun-23	AA+	A-1+	Stable	Reaffirmed
28-Jun-22	AA+	A-1+	Stable	Reaffirmed
29-Jun-21	AA+	A-1+	Stable	Reaffirmed
29-Jun-20	AA+	A-1+	Stable	Reaffirmed
26-Jun-19	AA+	A-1+	Stable	Reaffirmed
27-Jun-18	AA+	A-1+	Stable	Reaffirmed
02-Jun-17	AA+	A-1+	Stable	Initial

Due Diligence Meetings

Name	Designation	Date
Mr. S. M. Aamir Shamim	CEO & Managing Director	May 23, 2024
Mr. Abdul Jaleel Shaikh	Chief Risk Officer	
Ms. Humaira Siddique	Chief Financial Officer	
Mr. Adnan R. Naqvi	Group Head Corporate & Investment Banking Group	
Mr. Mustapha Ali Baig	Head – Treasury & Capital Markets	