

## Shelter Afrique

Rated Entity	Rating class	Rating scale	Rating	Outlook/Watch
Shelter Afrique	Long term Issuer	International	B-	Stable Outlook
	Short term Issuer	International	B	
	Long term Issuer	National	A+(KE)	Stable Outlook
	Short term Issuer	National	A1(KE)	
	Long term Issuer	National	AA(NG)	Stable Outlook
	Short term Issuer	National	A1+(NG)	

### Strengths

- Strong mandate, with expected improvement in track-record, of providing affordable housing in Africa.
- Well capitalised despite weak earnings.

### Weaknesses

- Modest size is a relative strain to self-fund very large housing projects.
- A chequered history of timely member support and limited preferential creditor treatment.
- Weak asset quality relative to rated peers.
- Modest funding structure versus supranational peers

### Rating rationale

The ratings on Shelter Afrique ('the company') balance the geographical distribution of the development book, with a chequered history of timely member support and limited preferential creditor treatment ('PCT'), the relatively modest size and diversity of the organisation and the strong underpin of the mandate. We also factor in the very robust capitalisation of the entity, despite weak earnings, poor asset quality (from the legacy book), moderate funding position versus supranational peers and adequate liquidity.

Shelter Afrique is a relatively small regional Multilateral Development Bank ('MDB') established with a mandate to provide affordable housing in Africa. Its modest size (with developmental exposures of just over USD164mIn at FY20) is a relative strain to its ability to self-fund very large developmental projects given a massive deficit of housing in Africa. The status of the institution is also constrained by some financial sustainability issues emanating from the disruptive event of 2016. This is reflected by core earnings which remain negative on the back of substantially low volumes in loan originations, although profitability has been on an improving trend supported by recoveries on the non-performing loan ('NPL') book. The company has a fairly diverse product range that addresses its housing mandate, with lines of credit and project finance having a meaningful impact.

We view the mandate to be strong, underpinned by the company's broad social, environmental, and economic development focus. Mandate strength is moderated for track-record that has diminished in recent years. With limited funding, the company's balance sheet contracted in the last three years, increasing replaceability risks for the institution in our opinion. Nonetheless, the company's non-financial capacity building initiatives meant to assist member

countries formulate appropriate affordable housing policy frameworks and provide technical expertise supports the institution's relevance to its shareholders, in our opinion.

The company's balance sheet is exposed to the operating environment risks of Africa. We believe these risks, which reflects the direct and indirect impact of the COVID-19 pandemic, have somewhat constrained fiscal capacity of member countries. Furthermore, the track-record of timely support by the shareholders has not been supportive of a higher credit rating. The company has some examples of preferred creditor status from member countries but as most are post-default, the ratings would benefit from sustained reduction in NPLs and minimised length of time in recoveries as proof of preferential treatment.

With a GCR leverage of c.73% at FY20, capitalisation is very strong, and we expect the ratio to trend within familiar levels of between 70% and 75% over the next 12-18 months, balancing ramped up capital subscriptions, improving profitability with significant retention levels, and anticipated expansion of the loan book. Internal capital generation has improved thanks to the improved recovery prospects of the NPL book. However, core earnings are negative returning -1.8% of adjusted assets at FY20 but expected to improve to around -0.7% by end of FY21, supported by a 19% increase in net interest income, substantial increase in non-funded income, and improved cost run rate. The downside risk of a weak GCR leverage ratio is contained over the next 2 years, given stronger capital collection levels expected between USD10mln and USD20mln per year, which is more than adequate to sustain potential drag on earnings. Loan loss reserve coverage of 71% as of Dec 2020 is considered adequate and in line with peers and we expect coverage to improve to between 94% and 120% over the next 2 years based on anticipated loan growth and the company's historical total book provision coverage.

Asset quality is a ratings' weakness, reflected by credit losses that are relatively higher in comparison to peers through the cycle. Impairments were booked lower at 1.2% as of Dec 2020 but we expect an increase to around 1.5% and 2% over the next 2 years. NPLs are also very high largely attributed to the legacy portfolio but are expected to lower on the back of improved recoveries. Concentrations are moderate and in favourable range to that of peers, with top 20 loans accounting for c.65% of the loan book at FY20. On the other hand, the risk management policies of the company were revised in 2018/2019 to address historical failures. We remain conservative in our view of asset quality metrics trends in the future, with the effectiveness of the aforementioned changes yet to be tested. Market risk is minimal with limited equity investments, and FX lending risks are well managed by natural hedging and sale of excess FX holdings.

The Funding structure is moderate in comparison to peers, reflected by confidence sensitive funding that has restrictive covenants under the debt restructuring agreement. The funding base is less diverse, but we anticipate with some confidence that the diversification of funders will gradually improve back to historical structure. That said, the company has started engaging new funders, having secured close to USD20mln for the year 2021, with other funders in the pipeline. On the other hand, liquidity is adequate with the company comfortably meeting all outstanding debt maturities by 1.25x over the next 12 months. Liquid assets/total assets registered at 27% at Dec 2020 vs 15% internal minimum and expected to decline to around 20-21% over the next 12-18 months. However, our liquidity assessment also factors in low quality of liquid assets with majority of the bank placements sitting in lower tier banks.

### Outlook statement

The outlook is stable reflecting our expectation for capitalisation to remain at strong levels and cushion the risk of poor earnings. Alongside the above, we also expect asset quality and liquidity risks to be stable following the successful completion of the debt restructuring agreement. However, we view financial sustainability risks and vulnerabilities to be in the moderate range over the medium term, with core earnings in negative territory and business stability yet to be proven.

### Rating triggers

The ratings may benefit from an improving track record of shareholder support in terms of increased capital subscriptions and timeliness of that support. In addition, a growing development book, building back status, more examples of preferential treatment, improved core earnings, better than expected impairments would also be viewed positively. The ratings could be lowered if the company does not regain business and financial sustainability, mandate

track record continues to diminish on the back of a sustained reduction of the development book, substantial deterioration in capital, credit losses exceeding our expectations, and/or if there is an increase in funding and liquidity risks.

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## Related criteria and research

Criteria for the GCR Ratings Framework, May 2019  
 Criteria for Rating Supranational Institutions, May 2019  
 GCR Ratings Scale, Symbols & Definitions, May 2019  
 GCR Country Risk Scores, July 2021  
 GCR Financial Institutions Sector Risk Score, June 2021

## Ratings history

### The Company for Habitat and Housing in Africa

Rating class	Review	Rating scale	Rating	Outlook	Date
Long and Short-Term issuer	Initial/last	International	B-/B	Stable	May 2021
	Initial/last	National	A+(KE)/A1(KE)	Stable	May 2021
	Initial/last	National	AA(NG)/A1+(NG)	Stable	May 2021

## Analytical Entity: Shelter Afrique

Shelter Afrique (Legal name: The Company for Habitat and Housing in Africa) is a Pan African institution that is mandated to provide affordable housing in Africa. It has ownership of 44 African member states and 2 institutional shareholders. Domiciled in the Republic of Kenya, Shelter Africa was established in 1982 by act of parliament and granted privileges and immunities such as diplomatic and tax-exempt status in Kenya and other select member countries.

## Operating Environment

### Country and Sector risk

The country and sector risk assessment are anchored by Shelter Afrique's exposure to the operating environments of the African continent. We consider most African countries to be high risk based on low creditworthiness of the sovereigns, low GDP numbers, the less diversified structure of economies, less robust monetary policies in comparison to developed countries amongst other key factors. Naturally, country and sector risk scores for these countries (on a scale of 15) are very low to reflect this inherent risk. And while the company's loan book is fairly diversified across 14 countries, the country and sector risk scores (3 and 2,75 respectively) are skewed to reflect a heavy tilt to Kenya (32%) and some other East African countries such as Rwanda, Tanzania and Uganda making up another 20% at FY20. In addition, the book is also diversified to some Southern African countries like Zimbabwe and Zambia that have very low country and sector risk scores. Please refer to the most up to date country and sector risk scores and related rationale at [www.gcratings.com](http://www.gcratings.com).

### Membership strength and diversity

The company has grown its membership from 20 member states since its inception to the current 44. There are 3 membership classes; A- African states; B-Institutional investors; and C-non regional/African countries. Class A represent

80% shareholding while the balance is with Class B. There is no uptake for Class C shares at moment given the return expectations for investors in that class vs the company's current profitability position. We consider the shareholding to be diverse and there are some strong shareholders such as the African Development Bank and few investment grade member countries. However, it is of our opinion that benefits of this diversity has been limited due to a lack of timely support during the disruptive event of 2016 and low capital subscriptions until recently.

## Business Profile

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### Status and Diversity

#### Modest size and weak core earnings a relative strain to status

Shelter Afrique has a modest market position reflected by the size of its development book of just over USD164m at HY21. Lack of scale is a relative strain for the company to self fund very large housing projects in Africa and given the huge deficit for affordable housing on the continent, we believe its capacity to rapidly build status within this space is constrained. Exacerbating this, the company's core earnings remain negative from since 2017 when it defaulted on some of its debt obligations, resultantly leading to a contraction of the balance sheet. Positively, a successful completion of the company's reorganisation/restructuring in 2019 brought some positive result in terms of its corporate governance structure which has seen profitability, amongst other positive things, improving on the back of enhanced recovery/collection methods for its legacy NPL portfolio. Furthermore, Shelter Afrique's core advantage lies in the fact that it's uniquely positioned as the only Pan African institution mandated to provide affordable housing and with this it has the platform to mobilise long term funding that matches the tenor of these projects.

The company addresses housing needs through an adequately diverse product range comprising lines of credit; project finance; equity investments & joint ventures; Public Private Partnerships; technical assistance, trade finance; housing microfinance; and infrastructure financing. Lines of credit and project finance have a meaning impact by balance sheet representation, split 60/40 by loan book.

### Mandate and track-record

#### Strong mandate but with weak track record

We consider the mandate of the institution to be strong, underpinned by its social, environment and economic development focus. This is reflected in its alignment with most of the United Nations' 2030 sustainable development goals. Shelter Afrique's track record for fulfilling its mandate has historically been good although it weakened in recent years. The last development impact assessment carried out in 2020 shows that the company financed approximately 17,500 housing over the last 5 years. While this may have exceeded internal targets, we still consider this modest versus the impact of other supranational peers. As part of strategy to enhance delivery of mandate, the company invests in equity of mortgage refinance companies, while partnering with real estate developers to support demand and supply side.

In order to assist member states develop appropriate affordable housing policy frameworks, Shelter Afrique established a Centre of Excellence Unit which is solely dedicated to provide intellectual capacity through research and capacity building programmes. We believe this alongside the above are some of the initiatives the company is taking to fulfill its mandate and ultimately this ensures it remains relevant to its shareholders.

### Management and governance

Management and governance is considered neutral to the ratings. The company went through restructuring between 2017 and 2019 which led to improvements in its corporate governance. This included creation of new board committees focusing on strategy, investor relations, NPLs recoveries.

## Financial Profile

### Capital and Leverage

#### Robust capitalisation expected to be sustained despite weak earnings

The capitalisation of the bank is a positive ratings factor. GCR leverage registered very strong level of c.73% at FY20 and we expect the ratio to trade within 500bps of the revised range of 70%-75% over the next 12-18 months, balancing higher capital subscriptions, improving profitability with higher retention levels, and anticipated loan book expansion. Despite current weak earnings, we expect the robust capitalisation levels of the bank to be sustained throughout the outlook horizon, underpinned by our assumptions below.

Our forecast factors in the following over the next 12-18 months:

- Modest loan book growth for the first half of 2021 before substantial growth of 18% in second half going into 2022. We expect disbursements to be relatively higher than repayments.
- Pre-provision income to increase substantially from negative base, benefiting from loan underwriting income and a stable cost base.
- Provisions to increase by 20% and 5% in 2021 and 2022 respectively, based on the anticipated loan growth and the company's historical total book provision coverage. We therefore expect cost of risk to increase to between 1.3% and 2%.
- Core earnings to gradually improve from negative territory, as we forecast between -0.7% and -0.1% of adjusted assets.

Table 1:

	2022(f)	2021(e)	2020	2019	2018
GCR Total Capital to Total Assets (%)	75.00%	77.13%	73.13%	57.60%	46.50%
Core Earnings to Adjusted Assets (%)	-0.10%	-0.70%	-1.84%	-1.38%	-3.97%

### Risk

#### Weak asset quality relative to rated peers

Asset quality is weak, balancing the high NPLs, moderate loan concentrations, and above peer average credit losses. The bulk of NPLs (c. USD88mln representing 53% of loan book at FY20) are from the legacy portfolio which dominates the outstanding loans at review date. We expect NPLs to gradually come down on the back of 1.) improved recovery methods; 2.) new business will be dominated by lines of credit that historically have very low NPLs; and 3.) strengthened risk management policies and procedures. Credit loss ratio was down to 1.2% from the prior year and we expect it to be between 1.3% and 2% over the next 12-18 months in line with loan loss reserving expectations. Although the current credit losses are in line with rated peers, through the cycle they have registered above peer average, and we consider the nature of the company's lending (especially project finance which has weak track record for losses) as relatively riskier. Positively, loan concentrations are moderately low with top 20 loans accounting for c.65% of total loan book at FY20. Market risk is adequately managed although the impact of any downside movement can be significant given the current earnings profile.

Table 2:

	2022(f)	2021(e)	2020	2019	2018
New loan loss provisions to average customer loans (%)	1.3%	2.0%	1.2%	1.5%	4.5%
Loan loss reserves to non-performing loans (%)	119.7%	94.2%	71.1%	76.1%	--
Gross non-performing loans to average customer loans (%)	26.9%	36.4%	53.6%	51.0%	--

## Funding and Liquidity

### Less diverse funding sources, good liquidity but with funding risks remaining

Funding structure is moderate, balancing the fairly diverse funding sources of mostly wholesale with the moderating risks still remaining post the debt restructuring agreement of 2019. Our assessment factors in the confidence sensitive nature of funding which is ratings negative. Positively, the bank holds good levels of liquidity, with liquid assets representing c.27% of total assets at FY20 against internal minimum of 15%, although the ratio is expected to decline to around 20% over the next 2 years as the company is entering its growth phase. Liquidity is also good from a cash flow perspective. The company's 12 months forecast cash inflows (includes loan repayments, capital subscriptions, and NPL recoveries) covers total outstanding debt maturities by 1.25x at FY20.

## Comparative Profile

The comparative profile is a neutral component for the ratings.

### Callable capital

Callable capital is neutral to the ratings, as there is a chequered history of timely support from shareholders.

### Peer analysis

Peer analysis is neutral to the ratings.

## Rating Adjustment Factors

### Structural adjustments

No structural adjustments have been made to the ACE in arriving at the final ratings.

### Instrument ratings

Not applicable to the ratings.

## Risk Score Summary

Rating Components and Factors	Risk scores
<b>Operating environment</b>	<b>8.25</b>
Country risk score	3.00
Sector risk score	2.75
Membership Strength and Diversity	1.50
Preferential Creditor Treatment	1.00
<b>Business profile</b>	<b>(1.00)</b>
Status and diversity	(3.00)
Mandate and track record	2.00
Management and governance	0.00
<b>Financial profile</b>	<b>2.50</b>
Capital and leverage	5.00
Risk	(2.00)
Funding structure and liquidity	(0.50)
<b>Comparative profile</b>	<b>0.00</b>
Callable capital	0.00
Peer analysis	0.00
<b>Total Score</b>	<b>9.75</b>

## Glossary

Balance Sheet	Also known as Statement of Financial Position. A statement of a company's assets and liabilities provided for the benefit of shareholders and regulators. It gives a snapshot at a specific point in time of the assets the company holds and how they have been financed.
Capital	The sum of money that is invested to generate proceeds.
Cash Flow	The inflow and outflow of cash and cash equivalents. Such flows arise from operating, investing and financing activities.
Cash	Funds that can be readily spent or used to meet current obligations.
Covenant	A provision that is indicative of performance. Covenants are either positive or negative. Positive covenants are activities that the borrower commits to, typically in its normal course of business. Negative covenants are certain limits and restrictions on the borrowers' activities.
Debt	An obligation to repay a sum of money. More specifically, it is funds passed from a creditor to a debtor in exchange for interest and a commitment to repay the principal in full on a specified date or over a specified period.
Diversification	Spreading risk by constructing a portfolio that contains different exposures whose returns are relatively uncorrelated. The term also refers to companies which move into markets or products that bear little relation to ones they already operate in.
Exposure	Exposure is the amount of risk the holder of an asset or security is faced with as a consequence of holding the security or asset. For a company, its exposure may relate to a particular product class or customer grouping. Exposure may also arise from an overreliance on one source of funding. In insurance, it refers to an individual or company's vulnerability to various risks
Income	Money received, especially on a regular basis, for work or through investments.
Interest Cover	Interest cover is a measure of a company's interest payments relative to its profits. It is calculated by dividing a company's operating profit by its interest payments for a given period.
Interest	Scheduled payments made to a creditor in return for the use of borrowed money. The size of the payments will be determined by the interest rate, the amount borrowed or principal and the duration of the loan.
Issuer	The party indebted or the person making repayments for its borrowings.
Leverage	With regard to corporate analysis, leverage (or gearing) refers to the extent to which a company is funded by debt.
Liquidity	The speed at which assets can be converted to cash. It can also refer to the ability of a company to service its debt obligations due to the presence of liquid assets such as cash and its equivalents. Market liquidity refers to the ease with which a security can be bought or sold quickly and in large volumes without substantially affecting the market price.
Long Term Rating	See GCR Rating Scales, Symbols and Definitions.
Margin	A term whose meaning depends on the context. In the widest sense, it means the difference between two values.
Market	An assessment of the property value, with the value being compared to similar properties in the area.
Maturity	The length of time between the issue of a bond or other security and the date on which it becomes payable in full.
Operating Cash Flow	A company's net cash position over a given period, i.e. money received from customers minus payments to suppliers and staff, administration expenses, interest payments and taxes.
Rating Outlook	See GCR Rating Scales, Symbols and Definitions.
Risk	The chance of future uncertainty (i.e. deviation from expected earnings or an expected outcome) that will have an impact on objectives.
Short Term Rating	See GCR Rating Scales, Symbols and Definitions.
Short Term	Current; ordinarily less than one year.

## Salient Points of Accorded Ratings

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The credit ratings have been disclosed to Shelter Afrique.

The ratings were solicited by, or on behalf of, Shelter Afrique, and therefore, GCR has been compensated for the provision of the ratings.

Shelter Afrique participated in the rating process via virtual management meetings, and other written correspondence. Furthermore, the quality of information received was considered adequate and has been independently verified where possible. The information received from the entities and other reliable third parties to accord the credit ratings included:

- Audited financial results as at 31 December 2020;
- Budgeted financial statements for 2021;
- Latest internal and/or external audit report to management;
- A breakdown of facilities available and related counterparties; and
- Industry comparative data.

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