The Pakistan Credit Rating Agency Limited

THE BANK OF PUNJAB (BOP)

RATING REPORT

	NEW [DEC-17]	PREVIOUS [JUN-17]
Entity		
Long Term	AA	AA
Short Term	A1+	A1+
Outlook	Stable	Stable
Debt Instrument		
TFC I	AA-	
Outlook	Stable	Stable

DECEMBER 2017

Assets:

- The bank's liquidity, in terms of its Liquid Assets-to-Deposits and Borrowings ratio, strengthened on YoY basis, to 47% at end-Sep17 (end-Sep16: 45%), comprising pre-dominantly government entities.
- BOP's advances portfolio constitutes 45% of total assets at end-Sep17 (end-Sep'16: 41%)
- The ADR remained steady at 59% (end-Sep'16:57%).

Funding

- The main source of BOP's funding is its deposit base, constituting around 87% of the total liabilities at end-Sep 17.
- The bank witnessed a sizeable growth in its deposit base in recent years (end-Sep17 : PKR 505mln, end-Dec 16: PKR 453bln, end-Dec15: PKR 375bln)

Credit Risk

- The bank has a sizeable infected portfolio (end-Sep17: PKR 54bln) representing 19% of gross advances.
- The Government of Punjab has issued two Letter of Credit's, undertaking to inject necessary funds to meet the capital shortfall up to a maximum amount of PKR 14.15bln (net of tax 35%) within a period of 90 days after close of the year ending 31st December 2018, if the bank fails to make a provision of PKR 21.7bln or if there is a shortfall in meeting the prevailing regulatory capital requirements as a result of the said provisioning.

Performance

- The asset yield declined by 0.5% (end-Sep17: 6.7%, end-Dec16: 7.2%) Similarly, cost of funds witnessed a decrease (end-Sep17: 3.5%, end-Dec16: 3.8%), thereby reducing the spread by 20bps (end-Sep17: 3.2%, end-Dec16: 3.4%).
- Interest income, in absolute amount, grew by 11% due to increased volumes.
- Pre-provision operating profit increased to PKR 7.2bln (end-Sep16: 7.02bln).

Capital

- The Capital Adequacy Ratio (CAR) of the bank is on the rise i.e. 14.92% at end-Sep17 due to retained profits and issuing of TFCs of PKR 2.5bln.
- The equity base of the bank has been strengthened through the elimination of significant accumulated losses.
- Moreover, in March 2017, the board of directors approved issue of right shares for PKR 12 per share at a premium of PKR 2 per share. This equates to PKR 13bln. The bank received the total subscription amount in July 2017.

Term Finance Certificate:

- The bank in order to further augment the Tier II capital is issuing TFC-II worth PKR 5bln.
- The tenor of the instrument will be ten years from the date of the issue whereas the profit is based on 6M-KIBOR plus 95 bps per annum.

Business Strategy

- Going forward, the management envisages growth in deposit base by targeting low cost CASA deposits while bringing granularity in customer base through penetrating private sector deposits.
- Benefit derived from association with GoPb shall continue.

Profile

- The Bank of Punjab, established under the BOP Act 1989, is listed on Pakistan Stock Exchange (PSX). The bank operates a vast network of 536 branches as at end-Dec 17, mainly concentrated in Punjab. The Government of Punjab (GoPb) holds majority stake in BOP (58%), whereas the rest is widely dispersed.

Governance and management

- Mr. Naeemuddin Khan, the President of the Bank since Sep'08, has four decades of diversified banking experience and has been associated with reputed international and domestic banks during his career. The senior management consists of seasoned bankers.
- He is backed by a team of experienced professionals, most of whom have long association with the bank.

RATING RATIONALE

The rating reflects the improved risk profile of BOP. The bank's capitalization and hence, risk absorption capacity has witnessed sizeable uptick. Capital Adequacy Ratio (CAR) of the bank clocks in at 14.92% at Sep – 17. There has been an appreciable improvement in the bank's profitability, over the years, on the back of improved interest income and capital gains, supplementing its equity base. The bank witnessed reduction in the non-performing loans inherited by the current management, though further recovery is taking time. Moreover, continued support from the sponsors - the Government of Punjab (GoPb) - provides requisite fiscal space; fresh capital injection and Letters of Comfort (LOCs) against provisioning for certain infected exposures are valid till 2018. Association with GoPb has benefited the bank also in terms of a sustainable deposit base and capital injection. The bank has raised further capital through right issue. This, along with projected profits, provides due cushion against uncovered NPL's. The bank envisages growth in advances wherein the criteria is higher margins with sustained risk profile. Meanwhile, expansion in deposit base with low cost focus, while attracting a wide customer range, is on the cards.

KEY RATING DRIVERS

The rating is dependent on the financial risk profile of the bank, mainly emanating from sustenance of capital adequacy and continued healthy profitability trend inline with the management's plans. Meanwhile, improvement in asset quality and upholding better governance standards remain imperative.

DEBT INSTRUMENT

The tenor of the instrument is 10 years from the date of issue. Profit is based on 6M-KIBOR plus 95 bps p.a . The issue carries lock-in and loss absorbency clauses, as per Basel III capital regulations. Although regulatory benchmark for CAR is increasing, given the bank's past performance, future projections and dividend payout pattern, cushion to lock- in and loss absorbency clause is expected to remain comfortable.

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The Bank of Punjab (BOP)

BALANCE SHEET	30-Sep-17	31-Dec-16	31-Dec-15
	9MY17	Annual	Annual
Earning Assets			
Advances (Net of NPL)	279,389	238,968	193,272
Debt Instruments	7,493	4,695	7,098
Total Finances	286,882	243,664	200,370
Investments	223,009	194,712	168,610
Others	17,144	14,646	7,911
	527,035	**453,022**	**376,891**
Non Earning Assets			
Non-Earning Cash	36,195	36,438	28,905
Deferred Tax	6,873	6,480	7,906
Net Non-Performing Finances	17,734	23,434	26,461
Fixed Assets & Others	26,599	25,840	32,120
	87,402	**92,192**	**95,392**
TOTAL ASSETS	**614,436**	**545,214**	**472,284**
Interest Bearning Liabilities			
Deposits	505,204	453,220	374,961
Borrowings	52,699	44,329	57,236
	557,903	497,549	432,198
Non Interest Bearing Liabilities	20,487	19,811	17,408
TOTAL LIABILITIES	**578,390**	**517,360**	**449,605**
EQUITY (including revaluation surplus)	**36,046**	**27,855**	**22,678**
Total Liabilities & Equity	**614,436**	**545,214**	**472,284**

INCOME STATEMENT	30-Sep-17	31-Dec-16	31-Dec-15
Interest / Mark up Earned	24,748	29,674	31,266
Interest / Mark up Expensed	(13,721)	(17,430)	(20,199)
Net Interest / Markup revenue	**11,026**	**12,244**	**11,068**
Other Income	2,247	3,636	5,989
Total Revenue	**13,273**	**15,880**	**17,057**
Non-Interest / Non-Mark up Expensed	(7,497)	(8,464)	(7,666)
Pre-provision operating profit	**7,274**	**9,075**	**11,026**
Provisions	(1,990)	(1,025)	(3,496)
Pre-tax profit	5,283	8,050	7,529
Taxes	(2,123)	(3,192)	(2,781)
Net Income	**3,161**	**4,858**	**4,748**

Ratio Analysis	30-Sep-17	31-Dec-16	31-Dec-15
Performance			
ROE	15%	22%	27%
Cost-to-Total Net Revenue	56%	53%	45%
Provision Expense / Pre Provision Profit	27%	11%	32%
Capital Adequacy			
Equity/Total Assets	5%	4%	4%
Capital Adequacy Ratio as per SBP	14.9%	12.3%	10.5%
Funding & Liquidity			
Liquid Assets / Deposits and Borrowings	47%	47%	42%
Advances / Deposits	59%	58%	59%
CASA deposits / Total Customer Deposits	71%	71%	66%
Intermediation Efficiency			
Asset Yield	7%	7%	9%
Cost of Funds	3%	4%	5%
Spread	3%	3%	4%

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STANDARD RATING SCALES & 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 or 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**. "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.

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. Rating Watch may carry designation – Positive (rating may be raised, negative (lowered), or developing (direction is unclear). A watch should be resolved within foreseeable future, but may continue if underlying circumstances are not settled.

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'.

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, a suspended 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, or e) the entity/issuer defaults.

Regulatory and Supplementary Disclosure

Name of Issuer The Bank of Punjab (BOP)
Sector Banking | Commercial
Type of Relationship Solicited

Purpose of the Rating Independent Risk Assessment
Regulatory Requirement

Rating History

Dissemination Date	Long Term	Outlook	Action
30-Dec-17	AA	Stable	Maintain

Related Criteria and Research

Rating Methodology: Bank Rating Methodology
Debt Instrument Rating Methodology

Sector Research: Banking Sector - Viewpoint | Jun-17

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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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Purpose of the Rating Independent Risk Assessment
Regulatory Requirement

Rating History

Dissemination Date	Long Term	Outlook	Action
30-Dec-17	AA-	Stable	Maintain

Nature of Instrument	Size of Issue (PKR mln)	Tenor (yrs)	Trustee
TFC I	PKR 2.5bln	10	Pak Brunei Investment Company Limited

Related Criteria and Research

Rating Methodology
Bank Rating Methodology
Debt Instrument Rating Methodology

Sector Research
Banking Sector - Viewpoint | Jun-17

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