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 0.8% (end-Sep17: 6.2%, end-Sep16: 7.0%) Similarly, cost of funds witnessed a decrease (end-Sep17: 3.2%, end-Sep16: 3.8%), thereby reducing the spread by 20bps (end-Sep17: 3.0%, end-Sep16: 3.2%).
- 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. 12.6% (end-Jun16: 12%) 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 465 branches, 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 12.6% at June – 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.

BALANCE SHEET	30-Sep-17	31-Dec-16	30-Sep-16	31-Dec-15
	9MY17	Annual	9M16	Annual
Earning Assets				
Advances (Net of NPL)	279,389	238,968	217,014	193,272
Debt Instruments	7,493	4,695	8,206	7,098
Total Finances	286,882	243,664	225,221	200,370
Investments	223,009	194,712	200,583	168,610
Others	17,144	14,646	10,517	7,911
	527,035	**453,022**	**436,320**	**376,891**
Non Earning Assets				
Non-Earning Cash	36,195	36,438	33,636	28,905
Deferred Tax	6,873	6,480	6,243	7,906
Net Non-Performing Finances	17,734	23,434	24,801	26,461
Fixed Assets & Others	26,599	25,840	25,573	32,120
	87,402	**92,192**	**90,253**	**95,392**
TOTAL ASSETS	**614,436**	**545,214**	**526,573**	**472,284**
Interest Bearning Liabilities				
Deposits	505,204	453,220	420,464	374,961
Borrowings	52,699	44,329	59,833	57,236
	557,903	497,549	480,298	432,198
Non Interest Bearing Liabilities	20,487	19,811	19,165	17,408
TOTAL LIABILITIES	**578,390**	**517,360**	**499,463**	**449,605**
EQUITY (including revaluation surplus)	**36,046**	**27,855**	**27,110**	**22,678**
Total Liabilities & Equity	**614,436**	**545,214**	**526,573**	**472,284**

INCOME STATEMENT	30-Sep-17	31-Dec-16	30-Sep-16	31-Dec-15
Interest / Mark up Earned	24,748	29,674	21,931	31,266
Interest / Mark up Expensed	(13,721)	(17,430)	(13,025)	(20,199)
Net Interest / Markup revenue	**11,026**	**12,244**	**8,905**	**11,068**
Other Income	2,247	3,636	2,828	5,989
Total Revenue	**13,273**	**15,880**	**11,733**	**17,057**
Non-Interest / Non-Mark up Expensed	(7,497)	(8,464)	(5,853)	(7,666)
Pre-provision operating profit	**7,274**	**9,075**	**7,018**	**11,026**
Provisions	(1,990)	(1,025)	(982)	(3,496)
Pre-tax profit	5,283	8,050	6,036	7,529
Taxes	(2,123)	(3,192)	(2,105)	(2,781)
Net Income	**3,161**	**4,858**	**3,931**	**4,748**

Ratio Analysis	30-Sep-17	31-Dec-16	30-Sep-16	31-Dec-15
Performance				
ROE	15%	22%	25%	27%
Cost-to-Total Net Revenue	56%	53%	50%	45%
Provision Expense / Pre Provision Profit	27%	11%	14%	32%
Capital Adequacy				
Equity/Total Assets	5%	4%	4%	4%
Capital Adequacy Ratio as per SBP	0.0%	12.3%	12.0%	10.5%
Funding & Liquidity				
Liquid Assets / Deposits and Borrowings	47%	47%	45%	42%
Advances / Deposits	59%	58%	57%	59%
CASA deposits / Total Customer Deposits	71%	71%	70%	66%
Intermediation Efficiency				
Asset Yield	6%	7%	7%	9%
Cost of Funds	3%	4%	4%	5%
Spread	3%	3%	3%	4%
Outreach				
Branches	465	453	453	406

The Pakistan Credit Rating Agency Limited

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.

Disclaimer: PACRA's rating is an assessment of the credit standing of an entity/issue in Pakistan. They do not take into account the potential transfer / convertibility risk that may exist for foreign currency creditors. PACRA's opinion is not a recommendation to purchase, sell or hold a security, in as much as it does not comment on the security's market price or suitability for a particular investor.

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

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

Rating Analysts

Faraan Taimoor
faraan.taimoor@pacra.com
(92-42-35869504)

Jhangeer Hanif
jhangeer.hanif@pacra.com
(92-42-35869504)

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.

Disclaimer

Rating Shopping
PACRA maintains principle of integrity in seeking rating business.
PACRA has used due care in preparation of this document. Our information has been obtained directly from the underlying entity and public sources we consider to be reliable but its accuracy or completeness is not guaranteed.

PACRA shall owe no liability whatsoever to any loss or damage caused by or resulting from any error in such information.

Conflict of Interest
PACRA, 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 done by them
The analysts involved in the rating process do not have any interest in a credit rating or any of its family members has any such interest
The analysts and members of the rating committees including the external member members have disclosed all the conflict of interest, including those of their family members, if any, to the Compliance Officer PACRA

The analysts or any of its family members do not buy or sell or engage in any transaction in any security which falls in the analyst's area of primary analytical responsibility. This is, however, not applicable on investment in securities through collective investment schemes. PACRA has established appropriate policies governing investments and trading in securities by its employees
PACRA may provide consultancy/advisory services or other services to any of its clients or to any of its clients' associated companies and associated undertakings that is being rated or has been rated by it. In such cases, PACRA has adequate mechanism in place ensuring that provision of such services does not lead to a conflict of interest situation with its rating activities
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 ii) fee mandate - signed with the payer, which can be different from the entity
PACRA ensures that the credit rating assigned to an entity or instrument should 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

Surveillance
PACRA monitors all the outstanding ratings continuously and any potential change therein due to any event associated with the rated entity/ issuer, the security arrangement, the industry etc, is disseminated to the market, in a timely and effective manner, after appropriate consultation with the entity/issuer
PACRA reviews all the outstanding ratings on annual basis or as and when required by any stakeholder (including creditor) or upon the occurrence of such an event which requires to do so

PACRA initiates immediate review of the outstanding rating(s) upon becoming aware of any information that may be reasonable be expected to result in any change (including downgrade) in the rating

Reporting of Misconduct
PACRA has framed and implemented whistle-blower policy encouraging all employees to intimate the compliance officer any unethical practice or misconduct relating to the credit rating by another employees of the company that came to his/her knowledge. The Compliance Officer reports to the BoD and SECP

Confidentiality
PACRA has framed a confidentiality policy to prevent abuse of the non-public information by its employees and other persons involved in the rating process, sharing and dissemination of the non-public information by such persons to outside parties
Where feasible and appropriate, prior to issuing or revising a rating, PACRA informs the issuer of the critical information and principal considerations upon which a rating will be based and provide the opportunity to clarify any likely factual misperception or other matter that PACRA would wish to be made aware of in order to produce a fair rating. PACRA duly evaluates the response. Where in a particular circumstance PACRA has not informed the entity/issuer prior to issuing or revising a rating, it informs the entity/issuer as soon as practical thereafter

Prohibition

Probability of Default (PD)

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