



The Pakistan Credit Rating Agency Limited

Rating Report

BankIslami Pakistan Limited

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Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
22-Jun-2018	A+	A1	Stable	Maintain	-
13-Dec-2017	A+	A1	Developing	Maintain	YES
22-Jun-2017	A+	A1	Developing	Maintain	-
25-Oct-2016	A+	A1	Rating Watch- Developing	Maintain	-
06-May-2016	A+	A1	Developing	Rating Watch	-

Rating Rationale and Key Rating Drivers

The ratings reflect BankIslami's sustained risk profile. The bank has focused on high growth in terms of advances while aligning its deposit share. The asset yield has benefited as the bank continual expansion in the high profit segments: Car lease and Housing finance amongst others. The bank also restrained the quantum of high cost of deposits, rationalising its cost of funds. Hence, spread witnessed sustainability. The significant milestone is that the bank has achieved its pre-provisioning operational break-even. It is a good omen and will reflect positively on its profitability, going forward. The NPLs are a concern, especially the borderline cases. The bank is expected to revisit its strategy as the new CEO fully takes over.

The ratings require sustainable improvement in BankIslami's operational performance, in turn, maintaining positive trend in bottom-line. At the same time maintaining a strong capital adequacy while pursuing growth is important. Any downward spiral in profits, or incidence of non-performing assets with consequent impact on equity may negatively impact the ratings.

Disclosure

Name of Rated Entity	BankIslami Pakistan Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology Correlation between long-term and short-term rating scale(Jun-17),Methodology Bank Rating(Jun-17)
Related Research	Sector Study Commercial Bank(Jun-18)
Rating Analysts	Jhangeer Hanif jhangeer@pacra.com +92-42-35869504

BANK ISLAMI PAKISTAN LIMITED (BIPL)	
PROFILE	
Incorporated	2004
Profile	A small sized Islamic bank with the network of 330 branches.
Legal Status	Listed
Head Office	Karachi

INDUSTRY SNAPSHOT
The banking sector has experienced highest growth in terms of advances in 2017 over the last decade. As a consequence, there is mounting pressure on capital adequacy ratio of the banks. The challenge is exacerbated as the internal generation of capital (profits) are witnessing a dip. Some relief on income side is expected with recent uptick in interest rates.

OWNERSHIP

- BIPL has four prominent sponsors namely the JS Group (through Jahangir Siddiqui & Company Limited (JSCL), Mr. Ali Hussain and SAJ Capital Management Limited, Emirates NBD (through Dubai Bank PJSC), and Randeree family. All these have a collective holding of ~76% in the bank and predominantly direct the affairs of the BIPL's board.

GOVERNANCE

- BIPL's seven member board of directors (BoD) including CEO constitutes representatives of sponsoring groups. Currently, one from DCD group, two are independent directors and four are non-executive (including DCD representation).
- Mr. Ali Hussain, MD SAJ Capital Limited, is the Chairman of the Board.
- BIPL's shariah board comprises three leading Islamic scholars of the country, namely (i) Mufti Irshad Ahmad Aijaz, (ii) Mufti Muhammad Husain, and (iii) Mufti Javed Ahmed.

MANAGEMENT

- Mr. Hasan A Bilgrami, the President of the bank has been instrumental in the growth of the bank. He has been associated with the bank since its inception.
- Mr. Hasan A. Bilgrami, who had indicated his interest to pursue other professional interests, will remain available as an adviser to the bank till Dec-18. Mr. Syed Amir Ali has joined the bank as Deputy CEO in Apr-18. He will take up the CEOship in Oct-18. He is Chartered Accountant by qualification, carried a more than one decade experience mainly with Meezan Bank.
- Management team comprises seasonal professionals.

RISK MANAGEMENT

- The bank NPLs, owing to significant bad book of defunct KASB bank, remained controlled during the year it's evident through NPLs to Gross Advances ratio (1QCY18: 12.2%; CY17: 12.1%; CY16: 14.6%; CY15: 18.5%).
- Majority of the NPLs are provided leaving a manageable drag on equity (Net NPLs/Equity: 1QCY18: 37.3%; CY17: 33.6%; CY16: 22.2%; CY15: 15.3%).
- Advances' concentration in terms of top-20 increased significantly to 49% (CY16: 28%; CY15: 58%; CY14: 18%). Whereas, during CY17, advances mix was dominated by corporate sector (76%) followed by consumer banking (15%) and SME sector (4%).
- Owing to more growth in advances banks' ADR increased (1QCY18:70.0%; CY17: 66.5%; CY16: 50.4%; CY15: 46%).
- The bank's concentration, sector wise, is Whole sale and Retail Trade (29.73%), followed by Individuals (19.79%) and Power, Gas, Water, Sanitary (9.80%).
- BIPL's investment portfolio continued to be dominated by government securities (1QCY18: 97%; CY17: 95%; CY16: 94%; CY15: 94%). During CY17, Portfolio was mainly skewed towards GoP Ijarah sukuk.

Business Risk

- During CY17, the bank was able to maintain its spreads. Although shedding of higher cost deposits resulted into lower cost of funds, but proportion of decrease in assets' yield has nullified that effect.
- Though rise in other operating income supported the total revenue, though its share in the total revenue increased (CY17: 16%; CY16: 13%). Despite the small reversal in the provisioning, higher YoY operating expenses on account of acquired branches resulted in small pre-tax profit of PKR 157mln (CY16: PKR 844mln).
- Owing to the revised computation of tax return and reassessment of provision on the taxation, Bank booked a deferred taxation of PKR 1,547mln. In 1QCY18, BIPL made pre-tax profit of PKR 60mln. This was based on higher net revenue and sustained operational expenditure.
- Going forward, the bank aims to considerably expand its lending portfolio by funding through low cost deposits. The Bank focus would be on enhancing the yield on assets. Recovery from non-performing loans of defunct bank is also a priority. The bank is prioritizing the rated client lending in future. Going forward, minimum capital requirements and sustainability of market share by achieving sustainable growth will be of vital importance to the management.

CAPITAL & FUNDING

- During CY17, BIPL's customer deposits increased to PKR 158bln, up 14% YoY against 9% growth achieved by the industry. Nevertheless, the bank's deposit share in the system remained intact (1.3%).
- The bank would maintain focus on low cost deposits. CASA exhibited an increase (1QCY18: 73%; CY17: 73%; CY16: 70%), which bodes well for cost rationalization.
- Concentration in top 20 deposits improved (CY17: 29%, CY16: 39%).
- The bank's liquidity position is weakened as evident by Liquid assets to Deposits & Borrowing ratio (CY17: 26%; CY16: 32%) declined on YoY basis remained lower. However in 1QCY18, is increased to 46%, owing to increased investment in govt. securities.
- At end-Mar18, CAR is largely maintained at 14.4% with Tier I at 11.0%.



	31-Mar-18 3M	31-Dec-17 CY17	31-Dec-16 CY16	31-Dec-15 CY15
<i>PKR mln</i>				
BALANCE SHEET				
Earning Assets				
Advances	117,083	114,992	75,415	67,215
Debt Instruments	277	309	1,018	1,100
Total Finances	117,360	115,301	76,433	68,315
Investments	43,943	41,783	45,300	34,786
Others	6,531	22,174	28,359	39,824
	167,833	179,258	150,091	142,925
Non Earning Assets				
Non-Earning Cash	12,518	11,784	8,921	10,817
Deferred Tax	7,855	7,702	5,918	6,591
Net Non-Performing Finances	4,638	4,163	2,402	1,579
Fixed Assets & Others	13,227	13,258	13,514	12,319
	38,239	36,907	30,755	31,306
TOTAL ASSETS	206,402	216,165	180,847	174,231
Interest Bearing Liabilities				
Deposits	173,882	179,249	154,400	153,058
Borrowings	11,679	15,570	6,066	3,198
	185,561	194,819	160,466	156,256
Non Interest Bearing Liabilities	7,378	7,669	7,936	6,789
TOTAL LIABILITIES	192,939	202,488	168,402	163,044
EQUITY (including revaluation surplus)	13,463	13,676	12,445	11,186
TOTAL LIABILITIES & EQUITY	206,402	216,165	180,846	174,231
INCOME STATEMENT				
Profit / Return Earned	2,857	10,354	10,128	8,834
Return Expensed	(1,501)	(5,249)	(5,791)	(5,119)
Net Revenue	1,355	5,105	4,336	3,715
Other Income	197	964	638	570
Total Revenue	1,552	6,069	4,974	4,285
Other Expenses	(1,562)	(6,178)	(6,160)	(5,188)
Pre-provision operating profit	(10)	(110)	(1,186)	(903)
Provisions	70	267	2,030	631
Pre-tax profit	60	157	844	(272)
Taxes	(21)	1,406	(391)	76
Net Income	39	1,563	452	(196)
RATIO ANALYSIS				
Performance				
ROE	1.3% *	13.5%	4.3%	-2.4%
Cost-to-Total Net Revenue	102.8%	103.1%	126.7%	122.9%
Provision Expense / Pre Provision Profit	688.4%	243.4%	171.1%	69.8%
Capital Adequacy				
Equity/Total Assets	6.0%	5.7%	6.0%	5.9%
Capital Adequacy Ratio as per SBP	14.4%	14.5%	13.4%	12.3%
Funding & Liquidity				
Liquid Assets / Deposits and Borrowings	29.1%	26.1%	32.7%	27.1%
Advances / Deposits	70.0%	66.5%	50.4%	44.9%
CASA deposits / Total Customer Deposits	73.9%	73.1%	70.2%	67.1%
Intermediation Efficiency				
Asset Yield	6.6% *	6.3%	7.0%	7.6%
Cost of Funds	3.2% *	3.0%	3.7%	4.1%
Spread	3.5% *	3.4%	3.3%	3.5%
Outreach				
Branches	330	330	321	317
<i>Annualized*</i>				
BankIslami Pakistan Limited				
Jun-18				



ENTITY CREDIT RATING SCALE & DEFINITIONS

Credit rating reflects forward-looking opinion on credit worthiness of underlying entity; 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		SHORT TERM RATINGS	
AAA	Highest credit quality. Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments.	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.	
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.		
AA	Indicate very strong capacity for timely payment of financial commitments. This capacity is not significantly vulnerable to foreseeable events.		
AA-			
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.		
A			
A-			
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.		
BBB			
BBB-			
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.		
BB			
BB-			
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.		
B			
B-			
CCC	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.		
CC			
C			
D	Obligations are currently in default.		
Rating Watch	Outlook (Stable, Positive, Negative, Developing)	Suspension	Withdrawn
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.	Indicates the potential and direction of a rating over the intermediate term in response to trends in economic and/or fundamental business or 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'.	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.	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.
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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

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- (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.
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- (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)
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- (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)

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