The Pakistan Credit Rating Agency Limited

Rating Report

Faysal Bank Limited

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
25-Jun-2022	AA	A1+	Stable	Maintain	-
26-Jun-2021	AA	A1+	Stable	Maintain	-
26-Jun-2020	AA	A1+	Stable	Maintain	-
27-Dec-2019	AA	A1+	Stable	Maintain	-
27-Jun-2019	AA	A1+	Stable	Maintain	-
27-Dec-2018	AA	A1+	Stable	Maintain	-
28-Jun-2018	AA	A1+	Stable	Maintain	-
30-Dec-2017	AA	A1+	Stable	Maintain	-
22-Jun-2017	AA	A1+	Stable	Maintain	-

Rating Rationale and Key Rating Drivers

Faysal Bank has registered a remarkable journey towards becoming and achieving a full-fledged Islamic bank. This is important as it is first of its kind globally. Given a pertinent focus towards and demand for transition towards Islamic Banking in the country, Faysal Bank stands at a distinct advantage. The conversion process is expected to be completed over the short horizon. FABL opened 30 new Islamic branches and converted 65 branches to Islamic during CY21, increasing the Islamic branch network to 595 branches, making it the biggest network of dedicated Islamic Branches amongst all conventional banks in Pakistan. Moreover, the Bank has launched the first ever Tawaruq based Islamic Credit Card to target a large unserved customer base. The ratings take comfort from the Faysal Bank Limited's (FABL) association with a foreign business group – (Dar Al-Maal Al Islami Trust). The presence of sponsor’s nominees on the Board stands to provide it with the industry-specific working knowledge and strategic thinking capability. The Bank has also benefited from management stability over the past several years. FABL continued its focus on growth while maintaining its relative positioning among medium sized banks. The Bank has prudent deployment of assets for better yields and carefully planned loan book growth. The Bank has a continued focus on operational efficiency and despite an increase in its branch network, related costs remained in check. These initiatives have supported the Bank’s profitability and provided a cushion against risk absorption capacity. The bank recorded improved total income and growth in profitability. Going forward, positive trajectory should sustain. The management is cognizant of dynamic competition in the industry and is taking steps to strengthen FABL's positioning amongst medium-sized banks operating in Pakistan. FABL remains a highly capitalized commercial bank with a common equity tier 1 (CET-1) ratio of 15.7% as at Dec-21. Pakistan’s economy has gone through several varied phases in last two years due to the COVID19 pandemic. Banking sector continued to flourish with high profitability. Going forward, the macro-economic environment is beset with myriad challenges due to heightened interest rate, tightening of demand, rupee depreciation and higher inflation. This has repercussions for all segments of the economy.

The ratings are dependent on the Bank's ability to sustain improvement in its financial profile. This is important since most peer banks have gained in terms of their size and profitability matrix in recent years. Any material weakening in asset quality, in turn, putting pressure on the Bank's profitability and risk absorption capacity may have negative implications for the ratings.

Disclosure

Name of Rated Entity	Faysal Bank Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology | Financial Institution Rating(Jun-21),Criteria | Correlation Between Long-term & Short-term Rating Scales(Jun-21),Criteria | Rating Modifiers(Jun-21)
Related Research	Sector Study | Commercial Bank(Jun-22)
Rating Analysts	Sehar Fatima | sehar.fatima@pacra.com | +92-42-35869504

Profile

Structure Faysal Bank Limited (FABL) was incorporated on October 3, 1994 as a public limited company under the provisions of the Companies Ordinance 1984. Its shares are listed on Pakistan Stock Exchange (PSX).

Background FABL started operations in Pakistan in 1987, first as a branch set up of Shamil Bank of Bahrain and since 1994, as a locally incorporated bank under the present name. In the year of 2002, Al-Faysal Investment Bank, another group entity, merged into Faysal Bank Limited. In 2010, FABL acquired 99.37% shareholding of Royal Bank of Scotland (Pakistan) Limited (RBS).

Operations The Bank is mainly engaged in Conventional and Islamic Corporate, Commercial and Consumer banking activities. The Bank is operating through 606 branches (end-Dec'20: 575) and 2 sub-branches (end-Dec'20: 1) across Pakistan. The registered office of the Bank is located at Faysal House, St-02, Shahrah-e-Faysal, Karachi, Pakistan.

Ownership

Ownership Structure Ithmaar Bank B.S.C, a wholly owned subsidiary of Ithmaar Holdings B.S.C. is the parent company of the Bank, holding directly and indirectly 66.78% of the shareholding of the Bank. Dar Al-Maal Al-Islami Trust (DMIT), (ultimate parent of the Bank) is the holding company of Ithmaar Holdings B.S.C.

Stability HR committee designs succession planning policies for the CEO, key executives and General Managers. Internal successors are highlighted in addition to earmarking key potential external resources to ensure a robust pipeline across all levels at the Bank.

Business Acumen Ithmaar Holdings B.S.C. (Ithmaar Holdings) is a Bahrain-based holding company that is licensed and regulated as an investment company and is listed on the Bahrain Bourse, Boursa Kuwait and Dubai Financial Market. Ithmaar Holdings has a paid-up capital of US$ 757.69mln.

Financial Strength Ithmaar Holdings B.S.C. has an asset base of USD 9.0bln and equity of USD 37.8mln as at Dec-21. Ithmaar Holdings B.S.C. and its subsidiaries are engaged in a wide range of financial services including retail, commercial, investment banking, private banking, takaful and real estate development.

Governance

Board Structure The overall control of the Bank vests in the eleven-member Board of Directors (BoD) including the CEO. Ithmaar Bank, the key shareholder, is represented by six non-executive directors on the board who are nominees of Ithmaar Bank.

Members' Profile Mr. Farooq Rahmatullah, the Chairman, is a law graduate. He has extensive experience in diverse roles related to the oil and gas industry.

Board Effectiveness Board meetings are conducted at a regular intervals and minutes of the meetings are documented adequately. The BoD exercises close monitoring of the management's policies and the Bank's operations through board committees.

Financial Transparency The External Auditors of the Bank, A F Ferguson & Co., Chartered Accountants, issued an unqualified audit opinion pertaining to annual financial statements for CY21. Furthermore, the Board has set up an effective internal audit function that reports independently to the Board Audit & Corporate Governance Committee regularly on compliance with critical policies and procedures and recommends on amendments to these policies in line with the industry best practices.

Management

Organizational Structure The Bank has well-defined organizational structure. Operations are segregated into various departments wherein clear lines of responsibility are defined for each cadre.

Management Team Mr. Yousaf Hussain is the President & CEO since May-2017. Mr. Hussain has been associated with Faysal Bank since 2008 and has banking experience of over two decades. He is supported by a management team of well experienced and qualified individuals.

Effectiveness A Management Committee (MANCOM), comprising group heads, meets on a quarterly basis to review the performance of each division vis-à-vis set targets. The MANCOM also provides strategic input for setting direction of the Bank vis-à-vis economic environment and decides on implications of new business initiatives for the Bank.

MIS The Bank has a comprehensive reporting system for the management to keep track of activities. The Bank is using business intelligence software namely QlikView.

Risk Management Framework Risk Management Framework's primary objective is to ensure that risk taking activities are in line with the guidelines approved by the BoD and to protect the interests of the Bank's depositors and shareholders.

Business Risk

Industry Dynamics Pakistan's economy has gone through several varied phases in last two years. It was deeply impacted by the magnitude of the COVID19 pandemic. The economic activity revived afterwards and Pakistan posted a GDP growth rate of ~4.0% in FY21 after a contraction in economy of -0.4% in FY20 (GDP growth figures were revised after base year was changed from FY05-06 to FY15-16). Banking sector continues to flourish with high profitability. Banking sector weightage is approximately ~25% of the KSE 100 index. Total banking assets posted growth of ~19% YoY whilst investments surged by 21% YoY to PKR ~14.4trln (end-Dec20: PKR ~11.9trln). Gross Advances of the sector recorded growth (23%) to stand at PKR ~10.9trln (end-Dec20: PKR ~8.8trln). Non-performing loans witnessed slight uptick of 4% to PKR ~860bln. Capital Adequacy Ratio stood at 16.7% (regulatory requirement of 11.5%). During CY21, banking sector deposits enhanced to PKR ~21.6trln (grew by ~17%). Hence, ADR rationalized to 47% (end-Dec20: ~45%). Net profitability of the sector recorded at PKR ~267bln (CY20: PKR ~244bln); up 9% YoY. However, growth of equity base of the sector recorded meagre uptick of 0.8% YoY attributable to handsome dividend payout.

Relative Position FABL is a medium-sized bank with sustainable growth and has witnessed an increase of 13.2% in its customer's deposit to PKR 586bln (CY20: PKR 518bln).

Revenues During CY21, net mark-up earned of the Bank witnessed an increase of 5.3% and was reported at PKR 25.8bln (CY20: 24.5bln). The non-markup income of the Bank marginally increased by 3.3% YoY, clocking in at PKR 8.5bln (CY20: PKR 8.2bln). During 1QCY22, net interest income earned reported at PKR 7.2bln (1QCY21: PKR 5.4bln).

Performance During CY21, the Bank's yield on assets declined recorded at 8.1% (CY20: 10.2%). The Bank's cost of funds also reduced to 4.1% (CY20: 5.6%). , operating cost of the Bank increased by 5.8% to PKR 20.8bln (CY20: PKR 19.7bln). The Bank's profit after tax (PAT) grew by 25.2% to PKR 8.15bln in CY21 (CY20: PKR 6.5bln). During 1QCY22, asset yield and cost of funds rises to 8.9% and 5.2% respectively.

Sustainability Going forward, FABL plans to focus on mobilizing low-cost core deposits and enhancing business volume via branch outreach. As per the plans of the parent institution, FABL is at an advance stage to wholly convert to shariah compliant operations.

Financial Risk

Credit Risk During CY21, FABL's loan portfolio registered a growth of 20% to PKR 453bln (CY20: PKR 377bln). Advances to Deposit Ratio (ADR) of the Bank stood at 61.5%. NPLs were reported at PKR 23.4bln (CY20: PKR 26.2bln). As a result, Infection ratio also decreased to 5.6% (CY20: 7.7%). During 1QCY22, infection ratio was recorded at 5.5%. Loan loss coverage ratio was recorded at 87.8%.

Market Risk FABL's investment portfolio continues to be dominated (96.3%) by government securities. FABL's investment portfolio comprises 39.4% of total earning assets (CY21: PKR 297bln; CY20: PKR 213bln). During 1QCY22, investments were increased by 29.6% on YoY basis.

Liquidity And Funding Bank's liquidity position showed improvement as reflected in liquid ratio 46.1% (end-Dec20: 45.8%), supported by low-cost current account and savings account (CASA) deposits and CASA ratio was 74.9% for CY21. During 1QCY22, Liquidity of the bank was recorded at 45.9% (1QCY21: 44.5%).

Capitalization During CY21, equity base of the bank was recorded at PKR 65.8bln the Bank achieved a CAR of 17.5% (CY20: 18.7%) with contribution from Tier-1 capital (15.7%) and Tier-II (1.9%). During, 1QCY22, equity to total assets ratio was recorded at 7.1% (1QCY21: 8.2%). CAR has been reduced to 16.8% on YoY basis.

PKR mln

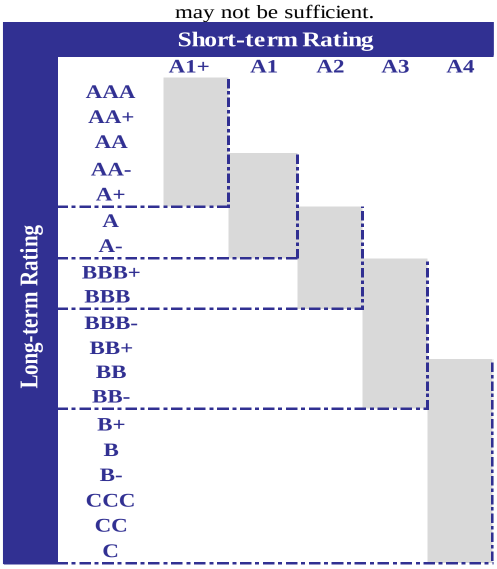
Faysal Bank Listed Public Limited	Mar-22 3M	Dec-21 12M	Dec-20 12M	Dec-19 12M
A BALANCE SHEET				
1 Total Finances - net	457,282	453,011	377,426	362,479
2 Investments	343,814	297,839	213,024	144,992
3 Other Earning Assets	10,473	4,415	6,846	5,381
4 Non-Earning Assets	117,850	111,430	108,002	110,829
5 Non-Performing Finances-net	2,847	2,917	4,660	6,172
Total Assets	932,266	869,612	709,958	629,853
6 Deposits	649,175	644,089	540,636	457,789
7 Borrowings	163,472	111,190	58,447	72,747
8 Other Liabilities (Non-Interest Bearing)	53,078	48,510	50,768	44,053
Total Liabilities	865,725	803,789	649,851	574,589
Equity	66,541	65,823	60,107	55,264
B INCOME STATEMENT				
1 Mark Up Earned	17,302	53,869	55,922	58,398
2 Mark Up Expensed	(10,120)	(28,035)	(31,388)	(37,278)
3 Non Mark Up Income	2,139	8,509	8,231	7,247
Total Income	9,321	34,343	32,765	28,367
4 Non-Mark Up Expenses	(5,967)	(20,887)	(19,740)	(17,333)
5 Provisions/Write offs/Reversals	147	(48)	(2,254)	(843)
Pre-Tax Profit	3,500	13,409	10,770	10,192
6 Taxes	(1,367)	(5,256)	(4,260)	(4,151)
Profit After Tax	2,133	8,153	6,511	6,041
C RATIO ANALYSIS				
1 Performance				
Net Mark Up Income / Avg. Assets	3.2%	3.3%	3.7%	3.4%
Non-Mark Up Expenses / Total Income	64.0%	60.8%	60.2%	61.1%
ROE	12.9%	12.9%	11.3%	12.2%
2 Capital Adequacy				
Equity / Total Assets (D+E+F)	7.1%	7.6%	8.5%	8.8%
Capital Adequacy Ratio	16.8%	17.5%	18.7%	19.1%
3 Funding & Liquidity				
Liquid Assets / (Deposits + Borrowings Net of Repo)	45.9%	46.1%	45.8%	36.5%
(Advances + Net Non-Performing Advances) / Deposits	62.2%	61.5%	58.9%	67.6%
CA Deposits / Deposits	41.3%	32.8%	30.7%	32.3%
SA Deposits / Deposits	37.9%	42.1%	40.4%	37.7%
4 Credit Risk				
Non-Performing Advances / Gross Advances	5.5%	5.6%	7.7%	9.1%
Non-Performing Finances-net / Equity	4.3%	4.4%	7.8%	11.2%

Credit Rating

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 Rating	
Scale	**Definition**
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 and in 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.** Substantial 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 Rating	
Scale	**Definition**
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
A4	The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions. Liquidity may not be sufficient.



**The correlation shown is indicative and, in certain cases, may not hold.*

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'.

Rating Watch Alerts to the possibility of a rating change subsequent to, or, in anticipation of some material identifiable event with indeterminable rating implications. But it does not mean that a rating change is inevitable. A watch should be resolved within foreseeable future, but may continue if underlying circumstances are not settled. Rating watch may accompany rating outlook of the respective opinion.

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, the rating should be considered withdrawn.

Withdrawn A rating is withdrawn on a) termination of rating mandate, b) the debt instrument is redeemed, c) the rating remains suspended for six months, d) the entity/issuer defaults., or/and e) PACRA finds it impractical to surveill the opinion due to lack of requisite information.

Harmonization A change in rating due to revision in applicable methodology or underlying scale.

Surveillance. Surveillance on a publicly disseminated rating opinion is carried out on an ongoing basis till it is formally suspended or withdrawn. A comprehensive surveillance of rating opinion is carried out at least once every six months. However, a rating opinion may be reviewed in the intervening period if it is necessitated by any material happening.

Note. This scale is applicable to the following methodology(s):

Entities
a) Broker Entity Rating
b) Corporate Rating
c) Financial Institution Rating
d) Holding Company Rating
e) Independent Power Producer Rating
f) Microfinance Institution Rating
g) Non-Banking Finance Companies (NBFCs) Rating

Instruments
a) Basel III Compliant Debt Instrument Rating
b) Debt Instrument Rating
c) Sukuk Rating

Regulatory and Supplementary Disclosure

(Credit Rating Companies Regulations,2016)

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

(3) No director, officer or employee of PACRA communicates the information, acquired by him for use for rating purposes, to any other person except where required under law to do so. | Chapter III; 10-(5)
(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 | Clause 11-(A)(p).
(8) PACRA prohibits its employees and analysts from soliciting money, gifts or favors from anyone with whom PACRA conducts business | Chapter III; 11-A-(q)
(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)
(11) PACRA promptly investigates, in the event of a misconduct or a breach of the policies, procedures and controls, and takes appropriate steps to rectify any weaknesses to prevent any recurrence along with suitable punitive action against the responsible employee(s) | Chapter III; 11-B-(m)

Independence & Conflict of interest

(12) 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 fee mandate - signed with the payer, which can be different from the entity
(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)

Proprietary Information