The Pakistan Credit Rating Agency Limited

Rating Report

Bank AL Habib Limited | Tier-I | TFC VI | Dec-17

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
29-Jun-2020	AA-	-	Stable	Maintain	-
28-Dec-2019	AA-	-	Stable	Maintain	-
28-Jun-2019	AA-	-	Stable	Maintain	-
31-Dec-2018	AA-	-	Stable	Maintain	-
28-Jun-2018	AA-	-	Stable	Maintain	-
06-Apr-2018	AA-	-	Stable	Harmonize	-
30-Dec-2017	AA	-	Stable	Initial	-
17-Nov-2017	AA	-	-	Preliminary	-

Rating Rationale and Key Rating Drivers

The rating reflects the bank's improved performance, exceptional asset quality, satisfactory financial profile and healthy liquidity. The bank has solidified its relative positioning in the universe of large sized banks by improving its market share in terms of deposit base and advances book. The bank continued with its strategy for outreach expansion - adding significant branches every year. Cost to total income declined during the year. The benefits are expected to unfold in coming days. The bank’s strong mark up income was further augmented by enhanced fee commission and foreign exchange income. The strength of the bank is reflected in the high proportion of retail deposits in the total. Hence, concentration is low and risk is reduced. The Bank grew its customers deposit base higher than the sector’s growth. Trade finance is the bank's hallmark. The rating draws comfort from the bank's experienced management team, prudent risk management policies and deep rooted relationship with clients - borrowers as well as depositors. NPLs slightly inched up, however, strong coverage is a positive. The bank has issued additional Tier-I and Tier-II instruments, augmenting the bank's CAR and providing room for growth. The bank's CET-I improved to 9.98% as at end Dec-19 (end Dec-18: 9.04%), and Total CAR improved to 14.35% as at end Dec-19 (end Dec-18: 13.43%). Covid-19 has posed challenges to the banking sector, as almost all segments of the economy, worldwide and domestically, are getting negatively impacted. The ramifications would continue to unfold, warranting vigilance and timely actions where needed.

The rating is dependent on the bank's sustained risk profile. In the wake of heightened competition, profitable growth is a challenge while retaining the relative positioning in the industry. The equity base of the bank and CAR are satisfactory and may continually be enhanced.

Disclosure

Name of Rated Entity	Bank AL Habib Limited | Tier-I | TFC VI | Dec-17
Type of Relationship	Solicited
Purpose of the Rating	Debt Instrument Rating
Applicable Criteria	PACRA_Methodology_FI(Jun-19),PACRA_Methodology_DI Basel III_FY19(Jun-19),Criteria | Rating Modifier(Jun-19)
Related Research	Sector Study | Commercial Bank(Jun-20)
Rating Analysts	Abdul Wahab | abdul.wahab@pacra.com | +92-42-35869504

Profile

Structure Bank AL Habib Limited (BAHL), incorporated as a public limited company, commenced operations as a Scheduled Commercial Bank in 1992. The bank is quoted on Pakistan stock exchange under the category of commercial banks.

Background The bank's registered office is located in the city of Multan in Punjab, its principal office is located in Karachi.

Operations The bank's principal activities are to provide commercial banking services to individuals and institutional clients. The bank has existing branch network of 755 branches /sub-branches, including 83 Islamic banking branches at end-Dec19.

Ownership

Ownership Structure Habib family and friends, associates and group companies owns major stake (end-Dec19: 49.96%) in BAHL. Other major shareholders include National Investment Trust (5.20%) and State Life Insurance Corporation (6.61%).

Stability Ownership structure of the bank is seen as stable as major stake rests with the sponsors.

Business Acumen The considerable experience and business acumen of the sponsors in commercial banking has been of value, as their background has allowed them to proactively deal with the changing dynamics of the industry and demonstrate consistent performance.

Financial Strength The sponsor's willingness to support the bank is considered high. Access to the capital markets is also a positive factor.

Governance

Board Structure Structure of BAHL's ten-member BoD includes three representative of Habib family while three are independent members.

Members' Profile The board members carry extensive professional experience in commercial banking, business and industrial sector.

Board Effectiveness There are five board committees; i) Audit Committee ii) Human Resource & Remuneration Committee, iii) Risk Management Committee iv) Credit Risk Management Committee and v) IT Committee which assist the board in effective oversight of the bank's overall operations on relevant matters. The BoD provides an overall guideline in managing risks associated with the bank's operations and strategic direction.

Financial Transparency The auditors of the bank, EY Ford Rhodes, Chartered Accountants, expressed an unqualified opinion on the bank's financial statements for the year ended December 31, 2019.

Management

Organizational Structure The bank has well-developed management tiers and succession plans for key management positions and a horizontal organizational structure, wherein the company's operations are grouped under various Division Heads.

Management Team Mr. Mansoor Ali Khan who is chief executive since November 2016, has been associated with the bank for more than 25 years. The strength of the bank comes from the core team of experienced senior banking professionals, having significant experience in banking, locally and abroad.

Effectiveness The bank has five internal committees in place at the management level to oversee its day-to-day operational matters and take decisions to implement the strategy outlined by the board. These include (i) Asset & Liability Management Committee (ALCO), (ii) Information Technology Steering Committee (ITSC), (iii) Operations Committee, (iv) Central Credit Committee (CCC) and (v) Compliance Committee of Management

MIS The bank is using in-house developed software named 'AL Habib Banking System - AHBS' as its core banking software that allows real-time on-line connectivity with other subsystems operating in the bank. The bank also has a separate Information Security Department.

Risk Management Framework BAHL has a robust risk management framework to manage various risks to which the bank is exposed. The overall responsibility of risk management lies with the BoD, through various committees of the board. The bank has in place a separate Risk Management Division (RMD).

Business Risk

Industry Dynamics As a result of general economic slowdown most indicators of the banking sector reflected mixed trend. Deposits of the banking sector stood at (CY19: PKR 15,953bln; CY18: PKR 14,254bln), showing a growth of ~12% as compared to 9.5% growth in CY18. Deployment of funds was largely skewed towards investments and particularly towards government instruments due to favorable interest rate dynamics (CY19: PKR 8,939bln; CY18: PKR 7,914bln). Meanwhile, advances witnessed a slowdown owing to subdued demand, cautious lending approach and monetary tightening .This was only a growth of 3.7% as compared to expansion of 22.2% in CY18. Asset quality saw deterioration – increased NPLs (CY19: PKR 761bln; CY18: PKR 680bln). The profitability of the banking sector improved due to an increase in Net Interest Income, which translated positively in other profitability indicators. The overall risk profile of the banking sector remained satisfactory.

Relative Position BAHL, a large sized bank, holds a good position in the industry with deposit base of PKR 904bln at end-Dec19 (about 6.2% market share).

Revenues During CY19, interest earned stood at PKR 105.6bln (CY18: PKR 60.7bln), up ~74% YOY on the back of volumetric growth in lending portfolio as well as peaked interest rates. Markup expenses increased by ~116% YOY (CY19: PKR 64.4bln; CY18: PKR 29.8bln). NIMR witnessed an increase of ~33% to stand at PKR 41.1bln (CY18: PKR 30.8bln). The bank's asset yield increased to 10.6% (end-Dec18: 7%). Cost of funds also increased to 6.2% (end-Dec18: 3.4%). Hence, Bank's spread augmented to 4.4% as of CY19 (CY18: 3.6%).

Performance During CY19, Non-markup income increased to PKR 9.5bln (CY18: PKR 7.3bln), up by ~30.5% YOY, mainly emanating from a significant increase in fees and commission income and foreign exchange income (CY19: PKR 6bln; CY18: PKR 4.8bln). The rise in non-markup expense by ~19.5% to stand at PKR 28.3bln (CY18: PKR 23.6bln) largely attributable to compensation and other operating expenses. The bank recorded net provisioning expense of PKR 3.4bln (CY18: PKR 247mln). Hence, bottom-line stood at PKR 11.2bln (CY18: PKR 8.4bln); recording robust growth of ~33% YOY.

Sustainability Going forward, BAHL envisages fortifying its market positioning; meanwhile, the focus is on enhancing its profitability via mobilization of low-cost deposits, expansion in branch network and achieving greater operational efficiency by keeping expenses under control and improving IT infrastructure. At the same time, selective diversification and monitoring of credit exposures would continue to remain an area of focus.

Financial Risk

Credit Risk During CY19, BAHL's advances have grown by 2.2% (CY19: PKR 489bln; CY18: PKR 478bln); below as compared to industry average (CY19: 3.7%). The Bank's ADR decreased to 54.1% (end-Dec18: 60%). Infection ratio witnessed slight uptick to ~1.5% end-Dec 19 (end-Dec18: ~1.1%).

Market Risk During CY19, BAHL invested majorly in government securities. Investment mix remains tilted towards long term government securities throughout the industry in the wake of rising interest rate environment.

Liquidity And Funding The bank's customer deposits posted a growth of 15% to stand at PKR 890bln (end-Dec18: PKR 773bln), against average industry growth of large banks (12%). CA deposits stood at PKR 440bln (end-Dec18: PKR 401bln) and SA deposits stood at PKR 265bln (end-Dec18: PKR 238bln) with CA and SA ratio of ~48.7 and ~29.4% respectively (CY18: 50.3% and 29.9%); whereas term Deposits was 21.9% (CY18: 19.7%).

Capitalization BAHL's paid-up capital stands at PKR 11.114 bln. However, the bank's equity base stand at PKR 61.5 bln (end-Dec18: PKR 49.5bln). BAHL has a CAR of 14.353% at Dec-19, (end-Dec18: 13.425%), with contribution from Tier I capital (11.238%) and Tier II capital (3.115%).

PACRA

PKR mln

Bank Al Habib Limited	Dec-19	Dec-18	Dec-17
Listed Public Limited	12M	12M	12M
A BALANCE SHEET			
1 Total Finances - net	496,494	485,705	346,237
2 Investments	580,855	409,651	472,065
3 Other Earning Assets	22,934	17,307	9,648
4 Non-Earning Assets	200,732	138,070	118,528
5 Non-Performing Finances-net	(2,333)	(2,495)	(2,344)
Total Assets	1,298,682	1,048,239	944,134
6 Deposits	903,740	796,901	692,576
7 Borrowings	243,738	134,034	144,497
8 Other Liabilities (Non-Interest Bearing)	89,701	67,752	61,184
Total Liabilities	1,237,179	998,687	898,258
Equity	61,503	49,552	45,876
B INCOME STATEMENT			
1 Mark Up Earned	105,602	60,733	50,309
2 Mark Up Expensed	(64,416)	(29,839)	(24,387)
3 Non Mark Up Income	9,481	7,268	8,118
Total Income	50,667	38,161	34,041
4 Non-Mark Up Expenses	(28,261)	(23,651)	(20,102)
5 Provisions/Write offs/Reversals	(3,395)	(247)	(49)
Pre-Tax Profit	19,011	14,264	13,890
6 Taxes	(7,842)	(5,846)	(5,389)
Profit After Tax	11,169	8,418	8,501
C RATIO ANALYSIS			
1 Performance			
Net Mark Up Income / Avg. Assets	3.5%	3.1%	3.1%
Non-Mark Up Expenses / Total Income	55.8%	62.0%	59.1%
ROE	20.1%	17.6%	19.2%
2 Capital Adequacy			
Equity / Total Assets (D+E+F)	4.7%	4.7%	4.9%
Capital Adequacy Ratio	14.4%	13.4%	13.8%
3 Funding & Liquidity			
Liquid Assets / (Deposits + Borrowings Net of Repo)	55.3%	49.7%	60.0%
(Advances + Net Non-Performing Advances) / Deposits	54.1%	60.0%	49.1%
CA Deposits / Deposits	46.5%	47.9%	51.9%
SA Deposits / Deposits	29.4%	29.9%	28.8%
4 Credit Risk			
Non-Performing Advances / Gross Advances	1.5%	1.1%	1.5%
Non-Performing Finances-net / Equity	-3.8%	-5.0%	-5.1%

Rating Scale | Debt Instrument

2019

Debt Instrument Rating Scale & Definitions

Credit rating reflects forward-looking opinion on credit worthiness of underlying 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 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 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.

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, a) some material identifiable event and/or b) deviation from expected trend. 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 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) cessation of underlying entity, c) the debt instrument is redeemed, d) the rating remains suspended for six months, e) the entity/issuer defaults., or/and f) 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.

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.
(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
(23) All information contained herein is considered proprietary by PACRA. Hence, none of the information in this document can be copied or, otherwise reproduced, stored or disseminated in whole or in part in any form or by any means whatsoever by any person without PACRA’s prior written consent

Regulatory and Supplementary Disclosure

Nature of Instrument	Size of Issue (PKR Bln)	Years	Security	Quantum of Security	Nature of Assets	Trustee	Book Value of Assets (PKR mln)
PPTFC-VI	7bln	Perpetual	Unsecured and subordinated as to payment of principal and profit to all other indebtedness of the bank, including deposits and will not be redeemable before maturity without prior approval of SBP	N/A	N/A	Pak Brunei Investment Co. Limited	N/A

Bank AL Habib Limited | Tier-I TFC VI | Dec -17

Due Date Principle	Opening Principal	Principal Repayment	Due Date Markup/ Profit	Markup/Profit Rate	6M Kibor (Assume 6M Kibor 10%)	Markup/Profit Payment	Installment Payable	Principal Outstanding
		PKR in mln						*PKR in mln*
Issuance	7,000	-						
May-18	Redemption Schedule not applicable since it's a perpetual TFC whereby there is no fixed or final redemption date. Profit (if declared) will be payable semi-annually in arrear, on a non-cumulative basis, on the outstanding TFC amount. The first such profit payable will fall due six months from the issue date and subsequently every six months thereafter subject to complying with regulatory requirements as stipulated in State Bank of Pakistan BPRD Circular No.6 dated August 15, 2013.		6 months from issuance	6 Month Kibor + 1.5%	10%	402.50	402.50	-
Nov-18			12 months from issuance	6 Month Kibor + 1.5%	10%	402.50	402.50	-
May-19			18 months from issuance	6 Month Kibor + 1.5%	10%	402.50	402.50	-
Nov-19			24 months from issuance	6 Month Kibor + 1.5%	10%	402.50	402.50	-
May-20			30 months from issuance	6 Month Kibor + 1.5%	10%	402.50	402.50	-
Nov-20			36 months from issuance	6 Month Kibor + 1.5%	10%	402.50	402.50	-
May-21			42 months from issuance	6 Month Kibor + 1.5%	10%	402.50	402.50	-
Nov-21			48 months from issuance	6 Month Kibor + 1.5%	10%	402.50	402.50	-
May-22			54 months from issuance	6 Month Kibor + 1.5%	10%	402.50	402.50	-
Nov-22			60 months from issuance	6 Month Kibor + 1.5%	10%	402.50	402.50	-
May-23			66 months from issuance	6 Month Kibor + 1.5%	10%	402.50	402.50	-
Nov-23			72 months from issuance	6 Month Kibor + 1.5%	10%	402.50	402.50	-
May-24			78 months from issuance	6 Month Kibor + 1.5%	10%	402.50	402.50	-
Nov-24			84 months from issuance	6 Month Kibor + 1.5%	10%	402.50	402.50	-
May-25			90 months from issuance	6 Month Kibor + 1.5%	10%	402.50	402.50	-
Nov-25			96 months from issuance	6 Month Kibor + 1.5%	10%	402.50	402.50	-
May-26			102 months from issuance	6 Month Kibor + 1.5%	10%	402.50	402.50	-
Nov-26			108 months from issuance	6 Month Kibor + 1.5%	10%	402.50	402.50	-
May-27			114 months from issuance	6 Month Kibor + 1.5%	10%	402.50	402.50	-
Nov-27			120 months from issuance	6 Month Kibor + 1.5%	10%	402.50	402.50	-