The Pakistan Credit Rating Agency Limited

Rating Report

Allied Bank Limited

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
27-Dec-2018	AAA	A1+	Stable	Maintain	-
06-Jul-2018	AAA	A1+	Stable	Upgrade	-
29-Dec-2017	AA+	A1+	Stable	Maintain	-
23-Jun-2017	AA+	A1+	Stable	Maintain	-
24-Jun-2016	AA+	A1+	Stable	Maintain	-

Rating Rationale and Key Rating Drivers

Allied Bank Limited is one of the top five banks of the country in terms of its deposit share. The bank's franchise, spread over a network of 1,258 branches, has enabled sustainable footprints into the country's deposit base. The bank's risk absorption capacity, as reflected in its sound equity base, has grown more than the market average over the years. This is supplemented by a significantly higher CAR (22.4% at end-Sep18), beyond the industry average. The bank has adopted a multi-faceted approach to augment its relative standing in the market. Increased attention is being diverted towards deepening of current business relationships and an enduring emphasis has been laid on building trade business. The bank's technology platform is a strength. This has facilitated fast and effective decision making while extending quality conventional and digital services to its customers. The related benefits would continue to unfold over the years. The bank remains focused on increasing its footprint in the market with consistent increase in number of branches / ATMs along with gradual penetration in digital banking. The ratings recognize the management's concerted efforts in sustaining the sound asset quality, while expanding its advances portfolio. The low infection ratio and high coverage ratio are considered positive. The concentration in lending portfolio is in line with bank's strategy of lending to large sized financially strong private groups and public sector entities. The continued strengthening in retail deposit market would enable further improvement in deposit granularity in terms of concentration as well as funding cost. At the same time, achieving efficiency in terms of utilization of its healthy CAR may help in further boosting ABL's market share and profitability.

The management's ongoing concerted efforts towards enhancing diversification in its revenue stream, achieving reduction in overall concentration, higher penetration in retail deposits and continuous improvement in cost structure remain important.

Disclosure

Name of Rated Entity	Allied Bank Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology | Financial Institution(Jun-18),Methodology | Criteria | Rating Modifier(Jun-18),Methodology | Correlation Between Long-Term And Short-Term Rating Scale(Jun-18)
Related Research	Sector Study | Commercial Bank(Jun-18)
Rating Analysts	Sehar Fatima | sehar.fatima@pacra.com | +92-42-35869504

Profile

Structure Allied Bank Limited (ABL), incorporated as a public limited company, commenced operations as a Scheduled Commercial Bank in 1942. The bank is quoted on Pakistan stock exchange under the category of commercial banks.

Background ABL was re-capitalized under a scheme of reconstruction by State Bank of Pakistan in 2004 and thereafter renamed Allied Bank Limited (ABL) in 2005. Since then, the bank has taken significant growth and has the fifth position in terms of deposit market share among large banks of Pakistan, at end-Sep18. It's head office is located in lahore.

Operations The Bank is engaged in commercial banking and related services. As of 9MCY18, ABL operates with 1,258 branches including 117 Islamic banking branches (31 December 2017: 1,250 branches including 117 Islamic banking branches) in Pakistan. ABL has a growing subsidiary – ABL Asset Management Company – which has AUM close to PKR 42.3bln at end-Sep18 (end-Jun18: PKR 42.1bln) with a market share of 6.4%.

Ownership

Ownership Structure Ibrahim Group (IG), through Ibrahim Holdings (Pvt). Limited owns 84% of shareholding in ABL. Previously, the same had been owned through Ibrahim Fibers Limited and sponsor family members. The rest is dispersed between individuals and corporates.

Stability Ownership structure of the Company is seen as stable as no ownership changes are expected in near future. Majority stake will rest with the Ibrahim Group.

Business Acumen The willingness towards the business is evident from the steadfast approach used by the management. Hence, sponsor's business acumen is considered strong.

Financial Strength Given that ABL is the flagship business of sponsors, willingness to support the bank in case the need arises is considered high; also supplemented by access to capital markets.

Governance

Board Structure The eight members BoD include the CEO, three sponsor directors, three independent directors and one non-executive director. Mr. Tahir Hassan Qureshi has been designated as the CEO since Jan-17. The Board now also includes one female director in compliance with regulatory requirements.

Members' Profile In accordance with requirements of Code of Corporate Governance (CCG), five members of BoD are "Certified Directors". Three directors have prescribed education and experience required for exemption from training programs of Directors pursuant to clause XI of CCG. The participation of all board members has remained high.

Board Effectiveness The board is currently assisted with five board committees. Namely, Audit, Risk, E-vision, Strategic Planning & Monitoring and Human Resource & Remuneration.

Financial Transparency Messrs KPMG Taseer Hadi and Company, Chartered Accountants expressed an unqualified opinion on the financial report for the year ended December 2017.

Management

Organizational Structure ABL is functionally divided into seventeen groups, each governed by respective chief and all reports to CEO. Company Secretary and Chief ARR report directly to BoD and Audit Committee of Board respectively.

Management Team Mr. Tahir Hassan, carrying over 29 years of banking experience, is the CEO of ABL since Jan-17. He has previously been associated with the bank in capacity of COO and CFO. Mr. Qureshi, FCA, has been associated with the bank for about last one decade. ABL has a management team of experienced executives.

Effectiveness The management operates through five committees at management level including 1) Management Committee (MANCO), 2) Assets & Liabilities Committee (ALCO), 3) AntiHarassment Committee (AHC), 4) Human Resources Committee (HRC) and 5) Central Administrative Action Committee (CAAC). MANCO is further assisted by Risk Management Committee, IT Steering Committee and Fair Treatment of Customers Committee.

MIS Comprehensive MIS reports are generated on daily, weekly and monthly basis which are viewed by management on regular basis.

Risk Management Framework The bank manages risk through a framework of sound principles, which includes an optimum organizational structure, and well-designed risk assessment and monitoring processes. The Risk Management Group (RMG) is mandated to implement this framework as a function working independently of business lines.

Business Risk

Industry Dynamics The banking industry witnessed significant expansion in the loan book. Last year and YTD (2018) both witnessed huge deployments. This is expected to slow down. New projects require gestation period and additionally crowding-out effect may take place. Rising interest rates mean profitability of the sector would take support. Yet NPLs, as a result, may also transpire. CAR is reaching the maximum requirement by December 2018 (11.9%). This will create a challenge for some of the players.

Relative Position ABL, a large sized bank, holds a good position in the industry with a customer deposit base of PKR 853bln at end-Sep18. (FY17: PKR 830bln).

Revenues During 9MCY18, ABL's interest earned increased to PKR 53bln (9MCY17: PKR 48bln). However, NIMR witnessed a meager increase of 0.3% on YOY basis. On the other hand markup expenses also increased by 20% YOY. The bank's asset yield remained largely same at 6.8% (end-Dec17: 6.8%). Cost of funds stood at 3.8% (FY17: 3.6%). Hence, Bank's spread inched down (9MCY18: 3.0%; FY17: 3.3%; 9MFY17: 3.3%).

Performance During 9MCY18, non-markup income recorded an increase of 41% YOY to stand at PKR 8.9bln (9MCY17: PKR 6.3bln) mainly emanating from an increase in unrealized gain on sale of investments (9MCY18: PKR 2,180mln; 9MFY17: PKR 410mln) and income from foreign currencies. The rise in non-markup expense (15%) stood at PKR 16,994mln (9MCY17: PKR 14,816mln) primarily due to the fact that bank has been expanding its branches. Bank recorded a reversal of PKR 1.2bln (Reversal: 9MFY17: PKR 1.2bln) which affected the bottom-line to stand at PKR 9.9bln (9MCY17: PKR 9.7bln). Earning assets increased by 1% (end-Sep18: PKR 1,086bln, end-Dec17: PKR 1,078bln) primarily due to surge in lending but decline in investment portfolio.

Sustainability Going forward, ABL continues focus in increasing its deposit base by leveraging its branch network and digitizing its products. Initiatives like mobile banking and branchless banking remain core to the strategy. Support would come from capitalizing recently upgraded IT infrastructure T-24; providing strategic edge to ABL. Bank envisages cautious approach towards lending growth to continue. Herein, concentration risk remains a key challenge.

Financial Risk

Credit Risk During 9MCY18, ABL's advances have grown by 14% (9MCY18: PKR 423bln; CY17: PKR 371bln). Growth in advances was slightly below industry average (9MCY18:15%). The Bank's ADR increased to 46% (end-Dec17: 42%). Whereby, infection ratio improved to ~4% end-Sep18 (end-Dec17: ~5%) on account of both increase in lending and decline in NPLs.

Market Risk During 9MCY18, ABL invested majorly in Government securities (88%) which are T Bills, whereas rest of the book (12%) is invested in strategic and non-strategic equity investments. ABL's exposure in Foreign Currency Bonds has increased to ~3% at end-Sep18 (end-Dec17: ~1%), while exposure in PIBs reduced to 16% at end-Sep18 (end-Dec17: 34%). This trend has been witnessed throughout the industry in the wake of rising interest rate environment in upcoming years.

Liquidity And Funding During 9MCY18, ABL's customer deposits increased to PKR 853bln (CY17: PKR 830bln), up 3% against 6% growth achieved by the industry. CASA proportion slightly inched up to 83% at end-Sep18 (end-Dec17: ~79%) driven by growth in CA deposits. The liquidity of the bank has remained within comfortable range since last few years. The (Liquid Assets / Deposits and Borrowings) ratio has remained at higher end of 70.4% (Dec17: ~73%). Coupled with a fairly stable and growing deposit base, liquidity management has not been a major concern for the bank.

Capitalization As at end-Sep18, the bank's equity base strengthened to PKR 82.6bln (end-Dec17: PKR 78bln) on account of consistent profitability. Hence, this augments the bank's leverage structure; equity outpacing that of assets. ABL's Capital Adequacy Ratio (CAR) is robust ((9MCY18: 22.4%), herein dominant portion is Tier-I (9MCY18: 17.6%) while TierII stood at 4.8%.

Allied Bank Limited

PKR mln

BALANCE SHEET	30-Sep-18	31-Dec-17	31-Dec-16	31-Dec-15
	9M	*Annual*	*Annual*	*Annual*
Earning Assets				
Advances	422,500	370,700	328,583	318,866
Debt Instruments	14,915	24,779	24,348	14,773
Total Finances	437,415	395,479	352,931	333,639
Investments	394,458	673,672	565,899	529,675
Others	254,273	9,343	11,193	7,706
	1,086,145	**1,078,494**	**930,023**	**871,020**
Non Earning Assets				
Non-Earning Cash	90,980	85,367	73,203	56,712
Deferred Tax	-	-	-	-
Net Non-Performing Finances	344	969	1,266	2,369
Fixed Assets & Others	78,011	80,882	65,123	61,566
	169,335	**167,218**	**139,591**	**120,646**
TOTAL ASSETS	**1,255,480**	**1,245,712**	**1,069,614**	**991,666**
Interest Bearning Liabilities				
Deposits	929,438	883,741	805,111	734,596
Borrowings	187,967	223,556	126,369	137,960
	1,117,406	1,107,297	931,480	872,556
Non Interest Bearing Liabilities	30,240	31,699	37,461	29,853
TOTAL LIABILITIES	**1,147,646**	**1,138,996**	**968,941**	**902,409**
EQUITY (including revaluation surplus)	**107,834**	**106,716**	**100,674**	**89,257**
Total Liabilities & Equity	**1,255,480**	**1,245,712**	**1,069,614**	**991,666**

INCOME STATEMENT	30-Sep-18	31-Dec-17	31-Dec-16	31-Dec-15
	9M	*Annual*	*Annual*	*Annual*
Interest / Mark up Earned	53,213	65,709	64,606	72,116
Interest / Mark up Expensed	(29,592)	(34,130)	(31,345)	(35,977)
Net Interest / Markup revenue	**23,621**	**31,578**	**33,261**	**36,140**
Other Income	8,892	8,872	11,210	9,755
Total Revenue	**32,513**	**40,450**	**44,471**	**45,895**
Non-Interest / Non-Mark up Expensed	(17,259)	(21,530)	(20,900)	(18,867)
Pre-provision operating profit	**15,254**	**18,921**	**23,571**	**27,028**
Provisions	1,156	1,958	260	(1,524)
Pre-tax profit	16,410	20,879	23,831	25,503
Taxes	(6,442)	(8,145)	(9,404)	(10,383)
Net Income	**9,968**	**12,734**	**14,427**	**15,120**

Ratio Analysis	30-Sep-18	31-Dec-17	31-Dec-16	31-Dec-15
	9M	*Annual*	*Annual*	*Annual*
Performance				
ROE	16.4%	16.6%	20.3%	23.3%
Cost-to-Total Net Revenue	52.3%	53.2%	47.0%	41.1%
Provision Expense / Pre Provision Profit	7.6%	10.3%	1.1%	-5.6%
Capital Adequacy				
Equity/Total Assets	6.6%	6.3%	7.0%	6.9%
Capital Adequacy Ratio as per SBP	22.4%	22.4%	20.8%	20.9%
Funding & Liquidity				
Liquid Assets / Deposits and Borrowings	70.4%	73.3%	73.7%	67.4%
Advances / Deposits	45.5%	42.1%	41.0%	43.8%
CASA deposits / Total Customer Deposits	81.7%	77.7%	76.0%	72.1%
Intermediation Efficiency				
Asset Yield	6.8%	6.8%	7.5%	9.4%
Cost of Funds	3.8%	3.6%	3.7%	4.6%
Spread	3.0%	3.3%	3.8%	4.8%
Outreach				
Branches	1,258	1,250	1,150	1,050

Rating Scale

Credit Rating Scale & 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.

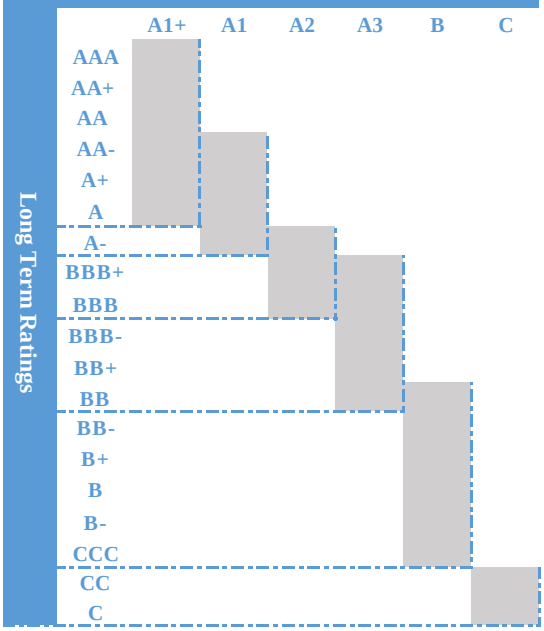
Long Term Ratings

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 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.

Short Term Ratings



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.

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