The Pakistan Credit Rating Agency Limited

Rating Report

Bank Alfalah 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	-
28-Dec-2019	AA+	A1+	Stable	Maintain	-
28-Jun-2019	AA+	A1+	Stable	Maintain	-
28-Dec-2018	AA+	A1+	Stable	Maintain	-
14-Jun-2018	AA+	A1+	Stable	Maintain	-
29-Dec-2017	AA+	A1+	Stable	Maintain	-
22-Jun-2017	AA+	A1+	Stable	Upgrade	-
30-Jun-2016	AA	A1+	Positive	Maintain	-

Rating Rationale and Key Rating Drivers

Bank Alfalah has built its franchise around its unique business proposition. The bank is an active player in the lending market. Its presence around different segments of advances book is also meaningful. The deposit growth that it has recorded also is a reflection of its well thought-out and well-implemented business model. The ratings reflect the bank's improved performance, good asset quality, strong financial profile and healthy liquidity. Asset quality improved as NPLs remained intact and overall infection ratio declined. In line with Bank’s overall Growth Strategy, Gross Advances of the Bank have increased by ~ 16% on YoY basis, contributing to increase in Risk Weighted Assets; along with regular dividend payouts during the year; thereby CAR stood at 14.43% (CY20: 16.53%). The Bank is adequately capitalized, with CAR level well above the Regulatory threshold. The bank's advances have improved to a notable level, resulting in a distinguished ADR (Net Advances to Deposits) of 59.2%, which is the highest among the universe of large banks. The mix of deposits largely remained the same. In terms of CA, the bank already has a distinct position among the leading banks. In line with the industry, BAFL's cost of funds also declined during 2021, which is attributed to the low policy rate for majority portion of the year and focus on building CASA book. Being customer centric bank, with focus towards technological advancement, BAFL has a sound foothold with a considerable presence across the country - enabling it to claim larger share in the ADC and digital transactions. PAT of the Bank increased by 35.7%. Effective implementation of the envisaged long term business strategy by the Bank has played an important role in business growth. The rating draws comfort from the Bank's stable ownership, experienced management team, prudent risk management policies and distinct emphasis on improving the position. Another dimension is digital banking initiatives (like Alfa Mall, ALFA Payment Gateway etc.), have been seeing growing throughput and profitability. Pakistan’s economy has gone through several varied phases in the 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 infection. This has repercussions for the entire system including banking.

The growth trajectory of the bank especially nurturing of the deposit & advances base and enriching the granularity would be considered positive.

Disclosure

Name of Rated Entity	Bank Alfalah 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 Bank Alfalah Limited (hereinafter referred as "BAFL" or "the Bank") was incorporated as a public limited company, in 1992, and is listed on Pakistan Stock Exchange (PSX).

Background Bank commenced operations in 1992. Since its inception, Bank Alfalah has grown rapidly to become Pakistan's one of the largest private commercial banks, the largest issuer and acquirer of credit cards, and one of the largest Islamic Banking businesses in the country. The Bank has a network of over 790 branches (including over 230 Islamic branches) as at end-Dec21.

Operations Bank provides financial solutions to consumers, corporations, institutions and governments through a broad spectrum of products and services, including corporate and investment banking, consumer banking and credit, commercial, SME, agri-finance, Islamic and asset financing.

Ownership

Ownership Structure BAFL is majority owned by Dhabi Group (49.79%), rest is owned by IFC (14.74%), Mutual funds, other NBFIs (24.57%) and General public (10.90%).

Stability Dhabi Group has retained the shareholding, since last many years and is expected to remain same in foreseeable future.

Business Acumen Dhabi group consists of some of the prominent members of UAE's ruling family and leading businessmen of UAE. The group has investments in countries including Pakistan, Bangladesh, Middle East, Europe and US.

Financial Strength Sponsors, having close ties with the ruling family of UAE, possess strong financial ability to support BAFL in case of need.

Governance

Board Structure At present, BAFL's board comprises of eight members including President/CEO and seven non-executive directors, out of which four are representatives of Dhabi Group and three members are independent.

Members' Profile Chairman of the board, H.H. Sheikh Nahayan Mabarak Al Nahayan, is a prominent member of the ruling family, UAE. Currently, he is UAE Cabinet Member and Minister of State for Tolerance and Coexistence.

Board Effectiveness To ensure effective and independent oversight of the Bank's overall operations, the Bank has constituted eight committees namely, i) Audit Committee, ii) Human Resource, Remuneration & Nomination Committee, iii) Risk Management Committee, iv) IT Committee, v) Strategy and Finance Committee, vi) Compensation Committee, vii) Real Estate Committee and viii) Crisis Management Committee.

Financial Transparency The external auditors of the Bank, EY Ford Rhodes, 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 Audit Committee.

Management

Organizational Structure BAFL has a lean organizational structure that clearly defines responsibilities, authority and reporting lines with proper monitoring and compliance mechanism.

Management Team Bank's senior management team comprises experienced bankers having national and international exposure. Mr. Atif Bajwa, joined Bank Alfalah as President and CEO in 2020. Mr. Bajwa has held numerous senior positions in large local and multinational banks, which includes: President/CEO of Bank Alfalah, President/CEO of MCB Bank and Soneri Bank.

Effectiveness Bank Alfalah has three main management committees for the purpose of strategic planning and decision-making under the Chairmanship of the CEO; (a) Central Management Committee; (b) Central Credit Committee; and (c) Digital Council.

MIS The Bank uses Temenos (T-24) as its core banking software across all branches.

Risk Management Framework The Board Risk Management Committee (BRMC) is appointed and authorized by the Board of Directors (BOD) to assist in design, regular evaluation and timely updating of the risk management framework of the Bank. The Board has further authorized management committees i.e., Central Management Committee (CMC) and Central Credit Committee (CCC) to supervise risk management activities within their respective scopes.

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 BAFL is ranked among the large banks of the country, on the basis of its strong growth trajectory in net advances and deposits. BAFL recorded one of the highest growth in customer deposits (21.0%) in CY21, among large banks. This led to increase in its system share to 5.2% (end-Dec20: 5.0%).

Revenues On the revenue front, net markup income for CY21 showed an increase of 3.0% to PKR 46.0bln (CY20: PKR 44.7bln). Non markup income showed an increase of 28.8% compared to last year, standing at PKR 16.5bln (CY20: PKR 12.8bln). The analysis revealed that during CY21, mix tilted towards mark up earned from investment (CY21: PKR 53.7bln; CY20: PKR 43.3bln) whilst mark up earned on advances recorded marginal attrition. This is attributable to low key policy rate which prevailed last year. During 1QCY22, the Bank earned the net markup income of PKR 14.3bln i.e. 38.4% higher than that of the corresponding period of last financial year (1QCY21: PKR 10.3bln).

Performance The Bank recorded an augmentation of 35.7% during CY21 in profit after tax, which stood at PKR 14.2bln as against PKR 10.5bln during CY20. The Bank's PBT for the year stands at PKR 23.4bln as against PKR 17.9bln during CY20, showing an increase of 30.7%.

Sustainability Looking ahead, Bank Alfalah is well-positioned for sustainable growth and building long-term shareholder value. The Bank will continue to invest in Digital Banking, in technology infrastructure, in human capital, and in strengthening compliance and controls environment.

Financial Risk

Credit Risk During CY21, net advances of the Bank increased by 17.3% on YoY basis to report at PKR 674.4bln (CY20: PKR 575.0bln). Net advances constitute around 38.9% of the Bank's total assets. At end Dec'21, the non-performing loan base of the Bank witnessed a decrease of PKR 1.2bln, and was reported at PKR 24.7bln. The infection ratio was recorded at 3.5% as compared to CY20 ratio of 4.3%; yet continuing to remain one of the lowest infection ratios in the industry.

Market Risk Following the significant investment in PIBs and T-Bills, the investment portfolio depicted an increase of 49.5%, amounting to PKR 787.1bln during CY21 (CY20: PKR 526.3bln). The government securities continue to dominate the overall investment book (90.4%). As at end Mar'22, investment portfolio increased by 11.9% to report at PKR 880.4mln.

Liquidity And Funding Total deposits were reported at PKR 1,139.0bln as of CY21 against PKR 881.8bln in CY20. Resultantly, ADR ratio (Net Advances to Deposits) decreased compared to last year as it stood at 59.2% in CY21 (CY20: 65.5%). During CY21, with a prudent approach BAFL has built a fair liquidity position; Liquidity coverage ratio of 172% (CY20: 187%) and Net stable funding ratio of 135% (CY20: 136%). As at end Mar'22, ADR (Net Advances to Deposits) further decreased to 58.3%. BAFL continue to carry a diversified deposit mix on the balance sheet with improved concentration levels.

Capitalization Bank's CAR as on CY21, stood at 14.43% (CY20: 16.53%), which is above the regulatory requirement of 11.50%. As at end Mar'22, CAR slightly improved to 14.77%.

PKR mln

Bank AlFalah Listed Public Limited	Mar-22 3M	Dec-21 12M	Dec-20 12M	Dec-19 12M
A BALANCE SHEET				
1 Total Finances - net	712,371	696,483	595,856	515,092
2 Investments	880,431	787,094	526,274	291,560
3 Other Earning Assets	28,274	48,064	101,387	87,143
4 Non-Earning Assets	228,482	203,163	159,080	167,834
5 Non-Performing Finances-net	(1,182)	(483)	2,276	3,682
Total Assets	1,848,376	1,734,321	1,384,874	1,065,311
6 Deposits	1,178,159	1,139,045	881,767	782,284
7 Borrowings	450,376	390,809	321,960	114,829
8 Other Liabilities (Non-Interest Bearing)	118,627	104,465	90,129	80,170
Total Liabilities	1,747,162	1,634,319	1,293,856	977,284
Equity	101,214	100,003	91,017	88,028
B INCOME STATEMENT				
1 Mark Up Earned	35,942	100,182	92,616	92,519
2 Mark Up Expensed	(21,653)	(54,134)	(47,911)	(47,623)
3 Non Mark Up Income	4,382	16,474	12,795	10,357
Total Income	18,671	62,522	57,499	55,253
4 Non-Mark Up Expenses	(10,444)	(36,840)	(32,032)	(29,843)
5 Provisions/Write offs/Reversals	(387)	(2,312)	(7,589)	(3,029)
Pre-Tax Profit	7,839	23,370	17,878	22,382
6 Taxes	(2,821)	(9,154)	(7,403)	(9,686)
Profit After Tax	5,019	14,217	10,475	12,696
C RATIO ANALYSIS				
1 Performance				
Net Mark Up Income / Avg. Assets	3.2%	3.0%	3.6%	4.3%
Non-Mark Up Expenses / Total Income	55.9%	58.9%	55.7%	54.0%
ROE	20.0%	14.9%	11.7%	15.5%
2 Capital Adequacy				
Equity / Total Assets (D+E+F)	5.5%	5.8%	6.6%	8.3%
Capital Adequacy Ratio	14.6%	14.4%	16.5%	16.9%
3 Funding & Liquidity				
Liquid Assets / (Deposits + Borrowings Net of Repo)	56.4%	54.4%	46.3%	42.6%
(Advances + Net Non-Performing Advances) / Deposits	58.3%	59.2%	65.5%	65.4%
CA Deposits / Deposits	46.5%	44.0%	44.7%	43.4%
SA Deposits / Deposits	34.1%	32.9%	33.2%	32.4%
4 Credit Risk				
Non-Performing Advances / Gross Advances	3.4%	3.5%	4.3%	4.2%
Non-Performing Finances-net / Equity	-1.2%	-0.5%	2.5%	4.2%

Credit Rating

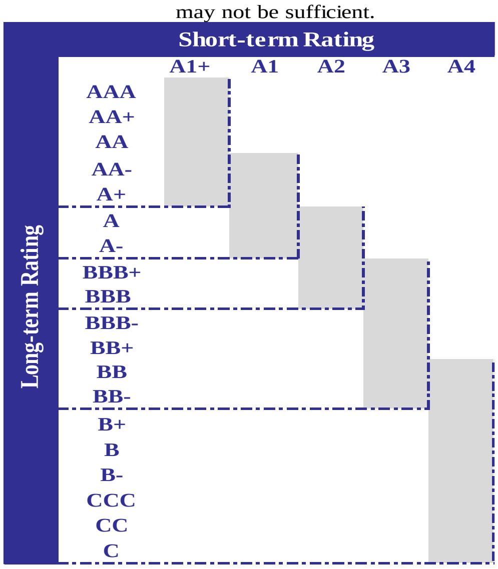
Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

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

Disclaimer: PACRA has used due care in preparation of this document. Our information has been obtained from sources we consider to be reliable but its accuracy or completeness is not guaranteed. PACRA shall owe no liability whatsoever to any loss or damage caused by or resulting from any error in such information. Contents of PACRA documents may be used, with due care and in the right context, with credit to PACRA. Our reports and ratings constitute opinions, not recommendations to buy or to sell.

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
(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