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
24-Jun-2023	AA+	A1+	Stable	Maintain	-
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	-

Rating Rationale and Key Rating Drivers

Bank Alfalah has strategically positioned itself in the lending market, capitalizing on its unique business proposition. The bank's presence in various segments of the advances book demonstrates its active role in the industry. Furthermore, the growth in deposits reflects the successful implementation of its well-planned business model. There is a sustained improvement in this ambit. The ratings highlight the bank's improved performance, strong financial profile, good asset quality, and healthy liquidity. As a customer-centric bank with a focus on technological advancement, Bank Alfalah has a strong nationwide presence, enabling it to capture a significant share in ADC and digital transactions. There has been a slight deterioration in asset quality as subjective non-performing loans increased, resulting in an infection ratio of 4% (CY21: 3.5%). Despite regular dividend payouts, the bank's Capital Adequacy Ratio stood at 13.83% (compared to 14.43% in CY21), indicating adequate capitalization above regulatory thresholds. The bank has achieved a notable level of advance, resulting in a distinguished Net Advances to Deposits Ratio (ADR) of 49.3% as at end-Dec'22. Bank Alfalah's growth strategy has led to an approximately 9.5% YoY increase in gross advances, contributing to an expansion in risk-weighted assets. The deposit mix has remained largely unchanged, and Bank Alfalah holds a distinct position among leading banks in terms of current accounts. The cost of funds increased in line with industry trends due to the prevailing high policy rate for the year. The bank's profitability has reflected significant growth, with a 28.1% increase in profit after tax (PAT). The effective implementation of the long-term business strategy, coupled with stable ownership, an experienced management team, prudent risk management policies, and a focus on improving its market position, provides confidence in the bank's performance. Additionally, Bank Alfalah's digital banking initiatives, such as Alfa Mall and ALFA Payment Gateway, have demonstrated growing throughput and profitability.
Pakistan's economy has traversed diverse phases in the past year, marked by political upheaval, an economic crisis, and devastating floods. The country has grappled with daunting challenges such as soaring inflation, currency depreciation, and precarious foreign reserves. However, the banking sector has persevered, showcasing high profitability. Looking ahead, the macroeconomic landscape is fraught with numerous challenges, including elevated interest rates, demand tightening, rupee depreciation, and heightened inflation, all reverberating across all economic sectors.

The bank's growth trajectory, particularly in terms of nurturing its deposit and advances base while enhancing granularity, is viewed positively.

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-22),Methodology | Correlation Between Long-term & Short-term Rating Scales(Jun-22),Methodology | Rating Modifiers(Jun-22)
Related Research	Sector Study | Commercial Bank(Jun-23)
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 Alfalah, established in 1992, has experienced remarkable growth to become a prominent private commercial bank in Pakistan. It holds a significant position in credit card issuance and acquisition, SME, digital banking, remittances and is recognized as one of the major players in Islamic Banking in the country. With an extensive network of 906 branches (including conventional, corporate, Islamic, and foreign branches), as well as 1,392 ATMs and CDMs/CCDMs, the bank operates across more than 200 cities in Pakistan as at end-Mar'23.

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 Bank Alfalah (BAFL) is majority-owned by the Abu Dhabi Group (The Group), with a stake of 56.16%. Other stakeholders include Mutual Funds, NBFCs, FIs, DFIs, individuals (43.69%), and executives (0.15%).

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

Business Acumen The 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, the Middle East, Europe, and the 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 Currently, BAFL's board consists of eight members, including the President/CEO and seven non-executive directors. Out of the seven non-executive directors, four represent the Abu Dhabi Group, while the remaining three members serve as independent directors.

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 retiring external auditors of the Bank, EY Ford Rhodes, Chartered Accountants, issued an unqualified audit opinion on annual financial statements for CY22. 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 include: President/CEO of Bank Alfalah, previously 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 and head office operations.

Risk Management Framework The Board Risk Management Committee (BRMC) is appointed and authorized by the Board of Directors (BOD) to assist in the 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 The country's economy has gone through several varied phases in the last few years. Looking ahead, the macroeconomic landscape is fraught with numerous challenges, including political instability, elevated interest rates, demand tightening, sizable rupee depreciation, and heightened inflation, all of which reverberate across all sectors of the economy. Pakistan posted a GDP growth rate of 6.10% in FY22 (GDP growth figures were revised after the base year was changed from FY05-06 to FY15-16). The banking sector continues to flourish with high profitability. Total banking assets posted growth of 18.5% YoY whilst investments surged by 25% YoY to PKR 18.0trln (end-Dec21: PKR 14.4trln). Gross Advances of the sector recorded growth (16%) to stand at PKR 12.6trln (end-Dec21: PKR 10.9trln). Non-performing loans witnessed an increase to PKR 924bln. The Capital Adequacy Ratio remained intact at 17% (regulatory requirement of 11.5%). However, declined in Mar-23 to 15%. During CY22, banking sector deposits enhanced to PKR 23.4trln. Hence, ADR rationalized to 50% (end-Dec21: 47%). CASA average, for the industry, stood at 74%. Net profitability of the sector was recorded at PKR 331bln (CY21: PKR 267bln); up 23% YoY. However, the growth of the equity base of the sector recorded a meager uptick of 7%YoY attributable to a handsome dividend payout.

Relative Position BAFL is a top-ranked bank known for its robust growth in net advances and deposits. It achieved the highest growth in deposits (31%) among large banks in CY22, raising its system share to 6.5% (end-Dec21: 5.4%).

Revenues In CY22, BAFL's markup earned increased to PKR 213.9bln (CY21: PKR 100.4bln). Net markup income surged by 66.9% to PKR 77.3bln (CY21: PKR 46.3bln). The asset yield rose to 12.3% (CY21: 7.3%), resulting in a spread of 4.5% (CY21: 3.3%). In 1QCY23, markup earned reached PKR 75.6bln, marking a 111.2% increase from 1QCY22 (PKR 35.8bln), and net markup income stood at PKR 27.9bln (1QCY22: PKR 14.3bln).

Performance In CY22, the Bank witnessed a 33.7% increase in non-markup income to PKR 21.8bln (CY21: PKR 16.3bln). Non-markup expenses rose by 37.2% YoY to PKR 50.5bln (CY21: PKR 36.8bln). Profit Before Tax at end-Dec'22 increased by 54.7% to stand at PKR 36.2bln (end-Dec'21: PKR 23.4bln), while profit after tax increased to PKR 18.2bln (Dec'21: PKR 14.2bln).

Sustainability Bank Alfalah is poised for sustainable growth and value creation in a challenging economic environment. The Bank will continue to invest in Digital banking, Technology, human capital, and compliance. The focus will be on expanding its network, building a low-cost deposit base, optimizing returns, and maintaining cost discipline. Prudent risk management practices will be followed amidst elevated interest rates and potential credit challenges.

Financial Risk

Credit Risk In CY22, Bank Alfalah's net advances grew by 8.7% to PKR 732.4bln (CY21: PKR 673.9bln). The non-performing loan base increased to PKR 30.9bln (CY21: 24.7bln), resulting in an infection ratio of 4% (CY21: 3.5%). The coverage ratio, including general reserve and subjective provisioning, improved to 107.6% in CY22 (CY21: 101.9%).

Market Risk Bank's investment portfolio (excluding non-government debt) surged by 38.8% to PKR 1,092.5bln in CY22 (CY21: PKR 787.1bln) where PIBs reached PKR 896.1bln (CY21: PKR 510.7bln). The bank incurred unrealized losses in CY22, mainly due to interest rate movement, which increased in 1QCY23.

Liquidity And Funding Total deposits of the Bank increased to PKR 1,486.8bln in CY22 from PKR 1,139.0bln in CY21. The Net Advances to Deposit Ratio (ADR) was recorded at 49.3% in CY22 (CY21: 59.2%). The CASA ratio decreased to 71.7% in CY22 (CY21: 76.9%). Total borrowings (including subordinated debt) increased to PKR 505.2bln in CY22 compared to PKR 390.8bln in CY21.

Capitalization Bank Alfalah maintained a Tier 1 capital of 11.09% in CY22, resulting in a CAR of 13.83% (CY21: 14.43%), exceeding the regulatory requirement of 11.50%. By the end-March'23, the CAR further improved to 14.66%.

PKR mln

Bank AlFalah Listed Public Limited	Mar-23 3M	Dec-22 12M	Dec-21 12M	Dec-20 12M
A BALANCE SHEET				
1 Total Finances - net	721,442	756,661	696,483	595,856
2 Investments	1,261,601	1,092,467	787,094	526,274
3 Other Earning Assets	224,610	117,750	48,064	101,387
4 Non-Earning Assets	325,727	288,665	203,163	159,080
5 Non-Performing Finances-net	(1,065)	(2,347)	(483)	2,276
Total Assets	2,532,315	2,253,197	1,734,321	1,384,874
6 Deposits	1,554,035	1,486,845	1,139,045	881,767
7 Borrowings	686,466	505,180	390,809	321,960
8 Other Liabilities (Non-Interest Bearing)	187,675	161,157	104,465	90,129
Total Liabilities	2,428,176	2,153,182	1,634,319	1,293,856
Equity	104,139	100,015	100,003	91,017
B INCOME STATEMENT				
1 Mark Up Earned	75,589	213,897	100,402	92,616
2 Mark Up Expensed	(47,652)	(136,558)	(54,134)	(47,911)
3 Non Mark Up Income	6,552	21,786	16,254	12,795
Total Income	34,489	99,126	62,522	57,499
4 Non-Mark Up Expenses	(14,993)	(50,497)	(36,840)	(32,032)
5 Provisions/Write offs/Reversals	(522)	(12,468)	(2,312)	(7,589)
Pre-Tax Profit	18,974	36,160	23,370	17,878
6 Taxes	(8,232)	(17,954)	(9,154)	(7,403)
Profit After Tax	10,743	18,206	14,217	10,475
C RATIO ANALYSIS				
1 Performance				
Net Mark Up Income / Avg. Assets	4.7%	3.9%	3.0%	3.6%
Non-Mark Up Expenses / Total Income	43.5%	50.9%	58.9%	55.7%
ROE	42.1%	18.2%	14.9%	11.7%
2 Capital Adequacy				
Equity / Total Assets (D+E+F)	4.1%	4.4%	5.8%	6.6%
Capital Adequacy Ratio	14.7%	13.8%	14.4%	16.5%
3 Funding & Liquidity				
Liquid Assets / (Deposits + Borrowings Net of Repo)	54.7%	56.6%	54.4%	46.3%
(Advances + Net Non-Performing Advances) / Deposits	44.9%	49.3%	59.2%	65.5%
CA Deposits / Deposits	43.7%	44.5%	44.0%	44.7%
SA Deposits / Deposits	24.3%	27.2%	32.9%	33.2%
4 Credit Risk				
Non-Performing Advances / Gross Advances	4.5%	4.0%	3.5%	4.3%
Non-Performing Finances-net / Equity	-1.0%	-2.3%	-0.5%	2.5%

Credit Rating

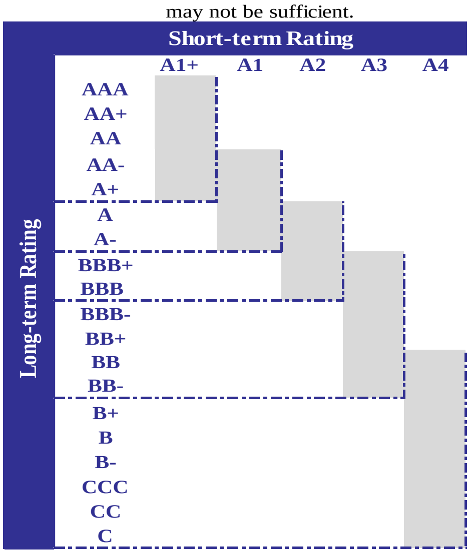
Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

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):

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

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