The Pakistan Credit Rating Agency Limited

Rating Report

The Bank of Punjab

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
18-Jun-2022	AA+	A1+	Stable	Maintain	-
18-Jun-2021	AA+	A1+	Stable	Upgrade	-
30-Jun-2020	AA	A1+	Stable	Maintain	-
28-Dec-2019	AA	A1+	Stable	Maintain	-
28-Jun-2019	AA	A1+	Stable	Maintain	-
27-Dec-2018	AA	A1+	Stable	Maintain	-
27-Jun-2018	AA	A1+	Stable	Maintain	-
30-Dec-2017	AA	A1+	Stable	Maintain	-
22-Jun-2017	AA	A1+	Stable	Maintain	-
23-Sep-2016	AA	A1+	Stable	Upgrade	-
29-Jun-2016	AA-	A1+	Positive	Maintain	-

Rating Rationale and Key Rating Drivers

The Bank of Punjab has built a franchise around its name, which itself is a reflection of strong parentage. The bank enjoys a respectable position in its peer universe, also reflected by its system share. The parentage of the bank has provided associated benefits to the institution. The management, led by the sound leadership, is poised to build on the strong foundations left by the previous management. The envisaged strategy encompasses a documented vision and defined road map to make a place for BOP in the top list of the banking industry. The incumbent management has revamped and strengthened governance and compliance structure in-place which is essential for oversight and dynamic operations of the Bank. The areas of focus envision three phases (control, consolidation & growth), which help lead the bank from augmented control environment to growth arena. Customer focus and geographical diversification and expansion are the key elements. The Bank grew its deposit base by 20.1% to stand at PKR 1,003bln - higher than the industry's growth where deposits remained tilted towards saving. The system share of the Bank has taken a positive contribution from the growth, which would lead the bank towards being classified as a large bank. The share of government and public sector deposit remain a challenge. During CY21, total net income of the bank displayed improvement primarily attributable to enhanced net markup income. Further, reversals of provisioning showed prudent asset management that augmented bank’s YOY net profit to increase by 79%, highest profit surge in the banking industry. Asset quality improved along with growth in advances. whereby the growth in risk assets will be covered through insurance and first loss guarantees wherever available. The top management is very much motivated and focused in further enhancing profitability and strengthening the Bank's relative position. There is a dilution in the CAR of the bank, prudent management of CAR is important. For this, the bank is in process of raising Tier 1 & Tier 2 capital, which is further expected to be supplemented by internal generation of capital.

The ratings are dependent on the financial risk profile of the bank, mainly emanating from volumetric increase in core operations and continued healthy profitability trend in line with the management's plans. Any weakening in asset quality will in turn put pressure on the bank's profitability and risk absorption capacity.

Disclosure

Name of Rated Entity	The Bank of Punjab
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 The Bank of Punjab (BoP) was established under the BoP Act 1989 (the Act), as a non-scheduled bank and was subsequently converted into a scheduled bank in 1994.

Background With its Head Office in Lahore, the Bank operates a network of 664 branches at end-Mar22 (end-Dec21: 662 branches) and employs 11,634 employees (end-Dec21: 11,257).

Operations The bank's principal activities are to provide commercial and islamic banking services to individuals and institutional clients. BoP entered Islamic Banking Operations in 2013, under the brand name of "Taqwa Islamic Banking". At end-Mar22, there are 115 (end-Dec21: 114) fully functional online Islamic Banking Branches.

Ownership

Ownership Structure The Government of Punjab (GoPb) holds controlling stake of 57.5% in bank of Punjab. The rest of shareholding is by local individuals (28.5%) and institutions (14.0%)

Stability Ownership structure of the bank is seen as stable as no ownership changes are expected in near future. Majority stake will rest with The Government of Punjab.

Business Acumen Sponsor's business acumen is considered good as BoP has been achieving milestones by successfully making the right business decisions. Over the last few years, it has sustained being a profitable institution.

Financial Strength BoP, being one of the flagship entities under umbrella of Government of Punjab, willingness to support the Bank in case the need arise is considered high; also supplemented by access to the capital markets.

Governance

Board Structure The control of the bank vests with eight-member Board of Directors comprising three non-executive directors, three independent directors and two executive directors. four members are representing Government of Punjab. Mr Zafar Masud – President of BoP is an executive director.

Members' Profile Members of BoD are also distinguished professionals including seasoned bankers and civil servants. However, owing to the institutional framework of BoP, the key shareholder can exert influence over the BoD that may potentially compromise its independence.

Board Effectiveness The BoD exercises close monitoring of the management's policies and the bank's operations via five sub-committees. Meetings for all these five committees are held quarterly. The Board members' attendance and participation is considered good and effective.

Financial Transparency The Audit Committee comprises four members; Mr. Muhammad Mudassir Amray is the chairman. The external auditors – M/s EY Ford Rhodes, Chartered Accountants, have expressed unqualified opinion on the financial statements of the bank for CY21.

Management

Organizational Structure The bank has long organizational structure with experienced senior management heading each function and/or unit and relevant segregation of duties in place.

Management Team Mr Zafar Masud is President and CEO. He has been associated with reputed international and domestic banks during his career. The senior management consists of seasoned bankers having diversified experience.

Effectiveness The bank has various committees in place at the management level to oversee its day-to-day operational matters and take decisions to implement the strategy outlined for it by the board. The committee, responsible for overseeing the operational matters of the bank, including human resource, different lines of business, compliance, and administration, meets fortnightly to review these areas.

MIS A comprehensive IT security policy has been put in place along with risk mitigation protocols. The bank has successfully implemented an internationally renowned Oracle based core banking system 'Flexcube" and all branches have been migrated to new CBS.

Risk Management Framework Risk Management Division (RMD), headed by Chief Risk Officer (CRO) – Mr. Arsalan Muhammad Iqbal manages different facets of risk including credit, market, operational, liquidity, reputation and country risk. Heads of Credit Risk Units – Corporate, Commercial, Consumer, Special Assets Management (SAM), and Agri – reports to head of credit risk, while heads of Operational, Market and Risk Policy reports directly to CRO.

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 BOP, a medium sized bank, secures a good position in the industry; 5% (end-Dec20: 4.9%) market share in terms of deposits. Customer deposit base stands at PKR 982bln as at end-Dec21 (end-Dec20: PKR 828bln).

Revenues During CY21, BOP's NIMR witnessed an incline of 28% on YoY basis to stand at PKR 29.8bln (CY20: PKR 23.3bln) primarily attributable to decreased mark-up expensed amounting to PKR 52bln (CY20: PKR 62.7bln) down by 21% YoY due to lower borrowings. Markup earned decreased by 5% YoY (CY21: PKR 81.6bln; CY20: PKR 86.0bln). Bank's asset yield declined and stood at 8.1% (end-Dec20: 10.0%). Cost of funds decreased marginally to 5.0% (CY20: 7.1%). Consequently, bank's spread inched up (CY21: 3.1%; CY20: 2.9%). During 1QCY22, NIMR increased by 18% YoY (1QCY22; PKR 8.1bln; 1QCY21: PKR 6.9bln). Spread stood at 3.2%.

Performance During CY21, non-markup income declined by 39% YoY (CY21: PKR 7.9bln; CY20: PKR 13bln). Non-markup expense also grew by 20% YoY standing at PKR 21.01bln (CY20: PKR 17.5bln). Net profitability recorded sizable improvement to 79% YoY and amounted to PKR 12.4bln (CY20: PKR 6.9bln) attributable to reversal booked of PKR 1.84bln (Provisioning expense in CY20: PKR 6bln). During 1QCY22, Net income grew by 17% to stand at PKR 2.1bln (1QCY21: 1.8bln) with respect to the corresponding period last year.

Sustainability The management envisages growth in deposit base while bringing granularity in customer base through further private sector deposits. Growth in advances is also on the cards, wherein the criteria is higher margins and sustainable risk profile. Implementation of modern technological tools would help in improving control regime and bringing efficiency in operation.

Financial Risk

Credit Risk At end-Dec21, BOP's net advances have grown by 23.7% YoY to stand at PKR 484bln (end-Dec20: PKR 391bln). ADR was reported at 48.3% (CY20: 46.8%). NPLs have decreased by 9% to stand at PKR 52bln (CY20: 57.2bln) Therefore, infection ratio improved to 9.7% (end-Dec20: 12.9%), reflecting positive on asset quality. Coverage ratio enhanced to 95.6% (end-Dec20: 90.1%). At end-Mar22, asset quality slightly improved further depicted by infection ratio of 9.5%.

Market Risk At end-Dec21, the investment portfolio of the bank has declined by 6% to stand at PKR 517bln, excluding debt instrument (end-Dec20: PKR 552.9bln). The composition of investment portfolio was 24% of T-Bills (end-Dec20: 58%), 71% of PIBs (end-Dec20: 37%) and 5% of other government securities and investments. Government securities constitutes 98.7% of total investment in CY21 (CY20: 99.3%).

Liquidity And Funding As at end-Dec21, customer deposits increased to PKR 982bln (end-Dec20: PKR 828bln), up by 18.5%. CA and SA proportion rationalized to 19.4% (end-Dec20: 18.2%) and 46.5% (end-Dec20: 47.2%) respectively. Furthermore, at end-Mar22, customer deposits increased to PKR 1,008bln with CA and SA proportion stood at 20% and 48.8% respectively.

Capitalization At end-Dec21, the bank reported CAR of 12.27% (CY20: 16.2%). At end-Mar22, Bank reported CAR of 11.6% (CAR 12.28% inclusive of ADT-I).

PKR mln

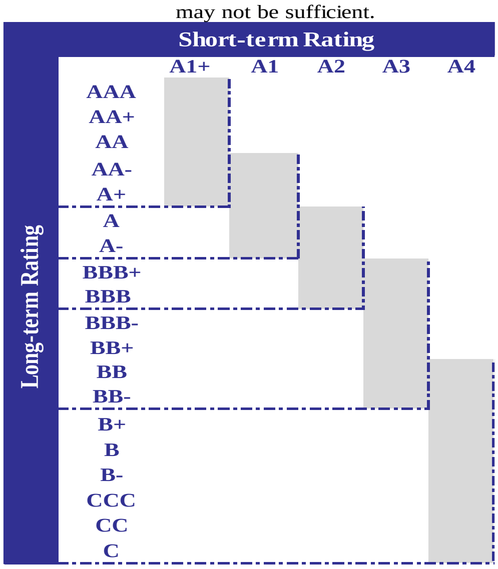
The Bank of Punjab Listed Public Limited	Mar-22 3M	Dec-21 12M	Dec-20 12M	Dec-19 12M
A BALANCE SHEET				
1 Total Finances - net	518,134	499,255	402,885	387,240
2 Investments	582,354	517,084	552,948	354,056
3 Other Earning Assets	16,333	40,207	18,807	8,491
4 Non-Earning Assets	147,479	140,656	117,690	115,671
5 Non-Performing Finances-net	11	(251)	3,116	3,470
Total Assets	1,264,312	1,196,952	1,095,446	868,928
6 Deposits	1,018,643	1,002,955	835,068	691,017
7 Borrowings	127,890	79,112	161,633	85,839
8 Other Liabilities (Non-Interest Bearing)	61,894	60,052	46,484	45,389
Total Liabilities	1,208,428	1,142,119	1,043,185	822,245
Equity	55,884	54,833	52,262	46,682
B INCOME STATEMENT				
1 Mark Up Earned	26,792	81,651	86,019	80,867
2 Mark Up Expensed	(18,680)	(51,775)	(62,694)	(54,110)
3 Non Mark Up Income	1,673	7,904	13,046	3,940
Total Income	9,786	37,780	36,371	30,696
4 Non-Mark Up Expenses	(7,366)	(21,014)	(17,519)	(14,876)
5 Provisions/Write offs/Reversals	1,064	1,642	(6,862)	(1,776)
Pre-Tax Profit	3,484	18,408	11,989	14,044
6 Taxes	(1,323)	(5,968)	(5,046)	(5,795)
Profit After Tax	2,161	12,440	6,944	8,249
C RATIO ANALYSIS				
1 Performance				
Net Mark Up Income / Avg. Assets	2.6%	2.6%	2.4%	3.4%
Non-Mark Up Expenses / Total Income	75.3%	55.6%	48.2%	48.5%
ROE	15.6%	23.2%	14.0%	19.5%
2 Capital Adequacy				
Equity / Total Assets (D+E+F)	4.4%	4.6%	4.8%	5.4%
Capital Adequacy Ratio	11.6%	12.3%	16.2%	14.8%
3 Funding & Liquidity				
Liquid Assets / (Deposits + Borrowings Net of Repo)	56.3%	55.2%	61.2%	53.1%
(Advances + Net Non-Performing Advances) / Deposits	49.4%	48.3%	46.8%	55.5%
CA Deposits / Deposits	20.0%	19.4%	20.3%	22.2%
SA Deposits / Deposits	48.8%	46.5%	47.3%	48.4%
4 Credit Risk				
Non-Performing Advances / Gross Advances	9.5%	9.7%	12.9%	12.0%
Non-Performing Finances-net / Equity	0.0%	-0.5%	6.0%	7.4%

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

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(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

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(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)

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(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)
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