The Pakistan Credit Rating Agency Limited

Rating Report

Bank Alfalah Limited | Additional Tier 1 TFC | PKR 7bln | Dec'22

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Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
14-Feb-2023	AA-	-	Stable	Initial	-
26-Sep-2022	AA-	-	Stable	Preliminary	-

Rating Rationale and Key Rating Drivers

Bank Alfalah Limited ("BAFL" or the "Bank") is an active player in the lending market. Its presence around different segments of advances book is also meaningful. The ratings reflect the Bank's performance, asset quality, strong financial profile and healthy liquidity. In line with the Bank’s overall growth strategy, as on Sep'22, the net advances of the Bank have increased by 15.3% YoY basis, contributing to increase in Risk Weighted Assets; along with regular dividend payouts, thereby CAR stood at 14.49% as of Sep'22 (CY21: 14.43%), well above the Regulatory threshold. The bank's advances have improved, However, the ADR (Advances to Deposits) decreased to 53.8% as of Sep'22 (Dec'21: 59.2%). Policy rates are continuously rising in CY22 increasing the Bank's cost of funds. PAT of the Bank increased by 34.4% and stood at PKR 14.1bln during 9MCY22 (9MCY21: PKR 10.5bln). In order to support the Bank's growth plans and expansion strategy, the Bank has issued additional tier-I capital amounting PKR 7bln. The additional tier-I is exposed to non-payment (principal & interest) risk in case the CAR falls below the minimum regulatory requirements. Being non-cumulative in nature, the interest payment falling due during that specific period wouldn't be paid to the investors as per the regulatory disclosures. Going forward, the macro-economic environment is beset with myriad challenges due to heightened interest rate, tightening of demand, rupee depreciation and higher infection.

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 | Additional Tier 1 TFC | PKR 7bln | Dec'22
Type of Relationship	Solicited
Purpose of the Rating	Debt Instrument Rating
Applicable Criteria	Methodology | Financial Institution Rating(Jun-22),Methodology | Debt Instrument Rating(Jun-22),Methodology | Rating Modifiers(Jun-22)
Related Research	Sector Study | Commercial Bank(Jun-22)
Rating Analysts	Muhammad Azmat Shaheen | azmat.shaheen@pacra.com | +92-42-35869504

Issuer Profile

Profile 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). Bank commenced operations in 1992. Since its inception, Bank Alfalah has grown rapidly to become one of the largest private commercial banks in Pakistan, 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 857 branches (including over 265 Islamic branches) as at Sep'22. 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 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%). Subsequent to the buyback of shares in Dec'22, the pattern of shareholding has changed. Dhabi Group has retained the shareholding, since last many years and is expected to remain same in foreseeable future. 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. Sponsors, having close ties with the ruling family of UAE, possess strong financial ability to support BAFL in case of need.

Governance 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. 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. 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. 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 BAFL has a lean organizational structure that clearly defines responsibilities, authority and reporting lines with proper monitoring and compliance mechanism. 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. 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. The Bank uses Temenos (T-24) as its core banking software across all branches. 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 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 after wards and Pakistan posted a GDP growth rate of ~4.0% in FY21. This revival was again hindered by flood disaster in FY22 and brought the post flood GDP down to ~2%. 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 14.9% whilst investments surged by 23.6% to PKR ~18.0trln in Sep'22 (end-Dec21: PKR ~14.5trln). Net Advances of the sector grew 9.2% to stand at PKR 11.1trln (end-Dec21: PKR ~10.1trln). Non-performing loans witnessed uptick to PKR 898bln. Capital Adequacy Ratio stood at 16.6% (regulatory requirement of 11.5%). The banking sector deposits closed to PKR 23.8trln at end-Sep'22. Hence, ADR rationalized to 46.4% (end-Dec21: 46.6%). Net profitability of the sector recorded at PKR 214bln YTD (9MCY21: PKR 192bln); up 11.5% YoY. However, growth of equity base of the sector recorded uptick of 6.6% YoY. BAFL recorded an increase in customer deposits by 21.5% to PKR 1,235bln (Dec'21: PKR 1,016bln). On the revenue front, net markup income for 9MCY22 showed an increase of 58.6% to stand at PKR 54bln (9MCY21: PKR 34bln). Non markup income showed a standing at PKR 17.5bln (9MCY21: PKR 11.4bln). The analysis revealed that during 9MCY22, mark up earned from investment increased by 137% to stand at PKR 84bln (9MCY21: PKR 35.4bln) whilst mark-up earned on advances recorded an increase of 64% (9MCY22: PKR 55.4bln; 9MCY21: PKR 33.8bln). The Bank recorded an augmentation of 34.4% during 9MCY22 in profit after tax, which stood at PKR 14.1bln as against PKR 10.5bln during 9MCY21. The Bank's PBT for 9MCY22 stands at PKR 27.6bln as against PKR 17.1bln during 9MCY21, showing an increase of 61.7%. Looking ahead, Bank Alfalah is well-positioned for sustainable growth and building long-term shareholder value.

Financial Risk As of Sep'22, net advances of the Bank increased by 10.5% to report at PKR 744.9bln (Dec'21: PKR 673.9bln). Net advances constitute around 34.1% of the Bank's total assets. At end Sep'22, the non-performing loan base of the Bank witnessed an increase of PKR 6.8bln and was reported at PKR 31.5bln (Dec'21: PKR 24.7bln). The infection ratio was recorded at 4.1% as compared to Dec'21 ratio of 3.5%. Following the significant investment in PIBs and T-Bills, the investment portfolio increased by 38.8%, amounting to PKR 1,123bln as of Sep'22 (Dec'21: PKR 809bln). The government securities continue to dominate the overall investment book. Total deposits were reported at PKR 1,385.4bln as of Sep'22 against PKR 1,139bln in Dec'21. Resultantly, ADR ratio decreased compared to last year as it stood at 53.8% as of Sep'22 (Dec'21: 59.2%). BAFL has built a fair liquidity position; Liquidity coverage ratio of 180% (Dec'21: 172%) and Net stable funding ratio of 137% (Dec'21: 135%). Bank's CAR as on Sep'22 stood at 14.5% (Dec'21: 14.4%), which is well above the regulatory requirement of 11.50%.

Instrument Rating Considerations

About The Instrument Bank Alfalah Limited issued an Additional Tier-I Term Finance certificate amounting to PKR 7bln. The instrument is privately placed and subsequently listed, unsecured, perpetual, non-cumulative and contingent convertible. The issue contributes towards supporting the Bank's Capital Adequacy Ratio (CAR) by strengthening additional Tier-I Capital as per guidelines set by SBP. Mark-up is payable semi-annually in arrears on outstanding principal amount @6MK+2.0%. The TFCs may be recalled and replaced with similar or better-quality capital, subject to SBP approval, after five years from the issue date on principal redemption date or thereafter, subject to call option condition. As per lock-in clause requirement, neither profit nor principal would be payable (even at maturity), if such payment will result in a shortfall in Bank's minimum capital requirement (MCR), leverage ratio (LR) or CAR or results in an increase in any existing shortfall in MCR, LR or CAR. Being non-cumulative in nature, the interest payment falling due during that specific period wouldn't be paid to the investors as per the regulatory disclosures. The TFC is subject to a loss absorbency clause, which upon the occurrence of Non-Viability event, SBP may fully or permanently convert the TFCs into common shares of the Bank.

Relative Seniority/Subordination Of Instrument The TFCs are subordinated to the payment of principal and profit, to all other indebtedness of the Bank, including deposits.

Credit Enhancement The instrument is unsecured.

PKR mln

Bank AlFalah Listed Public Limited	Sep-22 9M	Dec-21 12M	Dec-20 12M	Dec-19 12M
A BALANCE SHEET				
1 Total Finances - net	831,987	696,483	595,856	515,092
2 Investments	1,037,553	787,094	526,274	291,560
3 Other Earning Assets	26,618	48,064	101,387	87,143
4 Non-Earning Assets	290,678	203,163	159,080	167,834
5 Non-Performing Finances-net	(1,243)	(483)	2,276	3,682
Total Assets	2,185,594	1,734,321	1,384,874	1,065,311
6 Deposits	1,385,452	1,139,045	881,767	782,284
7 Borrowings	544,264	390,809	321,960	114,829
8 Other Liabilities (Non-Interest Bearing)	152,595	104,465	90,129	80,170
Total Liabilities	2,082,311	1,634,319	1,293,856	977,284
Equity	103,282	100,003	91,017	88,028
B INCOME STATEMENT				
1 Mark Up Earned	144,216	100,182	92,616	92,519
2 Mark Up Expensed	(90,205)	(54,134)	(47,911)	(47,623)
3 Non Mark Up Income	17,456	16,474	12,795	10,357
Total Income	71,467	62,522	57,499	55,253
4 Non-Mark Up Expenses	(35,688)	(36,840)	(32,032)	(29,843)
5 Provisions/Write offs/Reversals	(8,137)	(2,312)	(7,589)	(3,029)
Pre-Tax Profit	27,643	23,370	17,878	22,382
6 Taxes	(13,553)	(9,154)	(7,403)	(9,686)
Profit After Tax	14,090	14,217	10,475	12,696
C RATIO ANALYSIS				
1 Performance				
Net Mark Up Income / Avg. Assets	3.7%	3.0%	3.6%	4.3%
Non-Mark Up Expenses / Total Income	49.9%	58.9%	55.7%	54.0%
ROE	18.5%	14.9%	11.7%	15.5%
2 Capital Adequacy				
Equity / Total Assets (D+E+F)	4.7%	5.8%	6.6%	8.3%
Capital Adequacy Ratio	14.5%	14.4%	16.5%	16.9%
3 Funding & Liquidity				
Liquid Assets / (Deposits + Borrowings Net of Repo)	52.6%	54.4%	46.3%	42.6%
(Advances + Net Non-Performing Advances) / Deposits	53.8%	59.2%	65.5%	65.4%
CA Deposits / Deposits	43.6%	44.0%	44.7%	43.4%
SA Deposits / Deposits	30.4%	32.9%	33.2%	32.4%
4 Credit Risk				
Non-Performing Advances / Gross Advances	4.1%	3.5%	4.3%	4.2%
Non-Performing Finances-net / Equity	-1.2%	-0.5%	2.5%	4.2%

Credit Rating

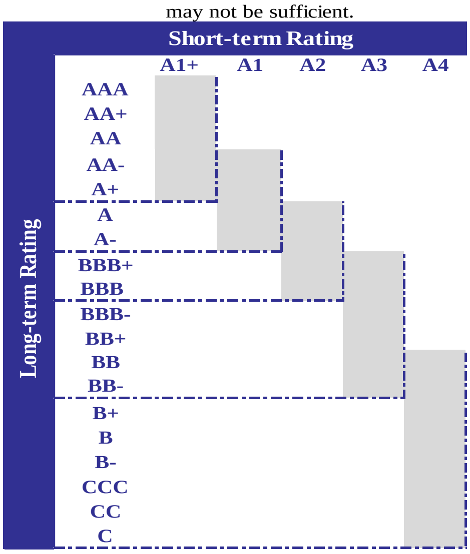
Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

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):

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)
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Regulatory and supplementary Disclosure

Nature of Instrument	Size of Issue (PKR)	Tenor	Security	Nature of Assets	Trustee
TFC - ADT 1	7 Bln	Perpetual	Unsecured and subordinated to all other obligations of the bank except ordinary shareholders.	N/A	Pak Brunei Investement Company Limited

Bank Alfalah Limited | TFC | Additional Tier I | PKR 7bln | Dec'22

Name of Issuer	Bank Alfalah Limited
Issue Date	21st December , 2022
Maturity	Perpetual (unless Call Option is exercised)
Profit Rate	6 months KIBOR + 2.00%
Call Option	Exercisable after 5 years from Issue Date
Principal Repayment	N/A
Security	Instrument will be unsecured and subordinated as to payment of principal and profit to all other claims except common shares.

Repayment Schedule

Opening Principal	Principal Repayment	Due Date Markup/ Profit	6M Kibor + 2.00%	Markup/Profit Payment	Installment Payable	Principal Outstanding
PKR in mln				*PKR in mln*		

Redemption Schedule not applicable since it will be a perpetual TFC whereby there will be no fixed or final redemption date. Profit (if declared) will be payable semi-annually in arrears, on a non-cumulative basis, on the outstanding TFC amount. The first such profit payment will fall due six months from the Issue Date and subsequently every six months thereafter subject to complying with regulatory requirements.
The instrument will carry a call option which may be exercised after 5 years from Issue date, subject to approval of the SBP.