The Pakistan Credit Rating Agency Limited

Rating Report

Habib Metropolitan Bank Limited

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
23-Jun-2023	AA+	A1+	Stable	Maintain	-
25-Jun-2022	AA+	A1+	Stable	Maintain	-
25-Jun-2021	AA+	A1+	Stable	Maintain	-
26-Jun-2020	AA+	A1+	Stable	Maintain	-
27-Dec-2019	AA+	A1+	Stable	Maintain	-
27-Jun-2019	AA+	A1+	Stable	Maintain	-
27-Dec-2018	AA+	A1+	Stable	Maintain	-
28-Jun-2018	AA+	A1+	Stable	Maintain	-
30-Dec-2017	AA+	A1+	Stable	Maintain	-

Rating Rationale and Key Rating Drivers

Habib Metropolitan Bank stands out for its formidable position in meeting trade-related needs and being a frontrunner in the industry. Its strong brand, skilled bankers, and strategic partnership with Habib Bank AG Zurich contribute to its success. As part of the House of Habib, HabibMetro has a significant presence in Pakistan's business sector, particularly in deposits and advances. In the reporting period, the bank experienced a remarkable 14.0% growth in deposits, primarily due to a notable 14.4% increase in current account deposits. The bank remains committed to optimizing its deposit mix through focused efforts. The overall infection ratio experienced an uptick, reaching 4.8% (compared to 4.0% in CY21). However, the bank has successfully reduced the non-performing loans (NPLs) over the years, as indicated by the recoveries made during the last three years. Furthermore, the bank maintains a coverage ratio of over 100%, demonstrating its ability to adequately provide for potential losses related to NPLs. Despite the increase in policy rates, the Bank has managed to improve its yields, resulting in increased spreads. This overall results in continuous improvement in return on assets (ROA) and return on equity (ROE) while keeping tax rates constant. Despite the improved influx of current account deposits, the bank’s cost of funds rose due to the upward adjustment of the policy rate in CY22, resulting in increased markup expenses. Nevertheless, the bank managed to incrementally improve its net markup income. This progress, combined with growth in non-interest income, enhanced profitability. Furthermore, the Bank maintained its non-markup expenses to total income ratio of 42% compared to Dec'21, despite the expansion made by the Bank. As of the end-Dec'22, the bank’s capital adequacy ratio (CAR) increased to 14.6% compared to 14.1% in CY21. Pakistan’s economy has faced various challenges over the past year, including political upheaval, an economic crisis, and devastating floods. The country has grappled with soaring inflation, currency depreciation, and precarious foreign reserves. Despite these difficulties, the banking sector has demonstrated resilience and maintained high profitability. However, looking ahead, the macroeconomic landscape presents numerous challenges, such as elevated interest rates, tightening demand, rupee depreciation, and increased inflation, affecting all sectors of the economy.

The ratings are contingent upon the management’s ability to strengthen the bank’s position in the banking industry as a whole and specifically in its market niche of trade finance, amidst rising competition. Any deterioration in asset quality would consequently impact the bank’s profitability and its capacity to absorb risks.

Disclosure

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

Background The Bank commenced its commercial-banking operations as Metropolitan Bank in October 1992; under this name, it remained a highly rated bank till October 2006, when the Bank merged with Habib Bank AG Zurich's Pakistan operations.

Operations Bank provides comprehensive banking services and products. These include specialized trade finance products, besides an array of products and technologically advanced services like mobile banking, globally accepted visa cards, and a nationwide ATM network. The Bank serves a wide range of corporate, retail, small business, agricultural, Islamic, and asset-financing customers.

Ownership

Ownership Structure HMBL is majorly owned by Habib Bank AG Zurich (HBZ) (51%), rest is owned by Corporates & FIs (30%) and Individuals (19%).

Stability The ownership structure has remained unchanged for many years and there is no expectation of any material change in the foreseeable future.

Business Acumen HMBL enjoys a close institutional relationship with Habib Group (HG) entities. Habib family, having been involved in banking for over 75 years, is considered the pioneer in introducing banking in Pakistan.

Financial Strength Habib Bank AG Zurich (HBZ) is a global financial institution with over 536 branches across eight countries on four continents. Owned and managed by the Habib Family, HBZ has three wholly owned subsidiary banks: Habib Bank Zurich Plc (UK), Habib Canadian Bank, and HBZ Bank Limited (South Africa). HBZ also has subsidiaries in Hong Kong (Habib Bank Zurich (Hong Kong) Ltd) and Pakistan (HMBL Pakistan).

Governance

Board Structure HMBL's Board of Directors (BoD) consists of nine members, including the CEO and three independent directors. Among the members, there are five non-executive directors, with three of them representing HBZ.

Members' Profile The chairman of the board, Mr. Mohamedali R. Habib is a well-known and seasoned banker with over 36 years' experience. He was appointed as Joint-President & Division Head (Asia) & Member of General Management of HBZ in 2011 and was elevated to Group CEO in 2016. He is accompanied by well-known and seasoned professionals.

Board Effectiveness The board actively participates in strategy formulation and effectively monitors the managerial affairs of the bank.

Financial Transparency KPMG Taseer Hadi & Co., Chartered Accountants, serves as the external auditors for the company and has provided an unqualified audit report on the annual financial statements for the year CY22. In addition, HMBL has established an Internal Audit Division that conducts ongoing reviews to enhance the quality of the bank's internal control environment.

Management

Organizational Structure HMBL's organizational structure and lines of authority are well-defined, with proper monitoring and compliance mechanism, and processes throughout the bank are largely governed by approved policies and procedures. The bank, with a largely horizontal organizational structure, has fifteen groups & divisions reporting to the CEO, except Internal Audit Division which reports to the Board's Audit Committee.

Management Team Mr. Mohsin Ali Nathani, the CEO, is a seasoned corporate banker with over 33 years of banking experience, covering Asia (East and South-East), the Middle East, and the Levant regions.

Effectiveness HMBL has various management committees including CMC, CCC, ALCO, Management Compliance Committee, BBRWG, and IT Steering Committee. These committees ensure smooth operations, coordinate at different levels, and maintain segregation of duties. An internal control framework is in place, regularly tested to address top risks and ensure effective oversight.

MIS HabibMetro continues to upgrade its core banking software, hPLUS. It offers many features including Intelligent Option Navigation, Event Monitoring, Real-Time Client Limit Monitoring, and Customer Credit Worthiness Analysis.

Risk Management Framework Prudent risk management aspects are embedded in the bank's strategy, organizational structure, processes, and systems and controls. The bank has adopted a cohesive management structure for credit, operations, liquidity, and market risk.

Business Risk

Industry Dynamics Pakistan's economy has gone through several varied phases in the last two years. The economic activity revived and Pakistan posted a GDP growth rate of ~6.10% in FY22. Total banking assets posted growth of ~19% YoY whilst investments surged by 26% YoY to PKR ~18trln (end-Dec21: PKR ~14trln). Gross advances of the sector recorded growth (16%) to stand at PKR ~12.6trln (end-Dec21: PKR ~9.0trln). Non-performing loans witnessed a slight uptick of 7% to PKR ~924bln. The capital Adequacy Ratio stood at 17.0% (regulatory requirement of 11.5%).

Relative Position During CY22, Bank's deposits (PKR 880bln) increased by 14%, as compared to the corresponding year when total deposits stood at PKR 772bln. HMBL retained its position in medium banks with a share in total customer deposits of the sector at 3.9% (CY21: 3.7%).

Revenues In CY22, HMBL reported a substantial increase in gross markup income, reaching PKR 133bln, an 82% rise compared to CY21's PKR 73bln. The net markup income grew by 38% to PKR 40.6bln (CY21: PKR 29.4bln). The asset yield increased to 11.4% in CY22 from 7.3% in CY21, driven by the rise in the key policy rate. The cost of funds surged from 4.5% in CY21 to 8% in CY22. Consequently, the overall spread improved to 3.4% in CY22 compared to 2.9% in CY21. The net markup income for 1QCY23 grew by 77.9% to PKR 13.7bln, compared to PKR 7.7bln in 1QCY22. The asset yield in 1QCY23 rose to 14.2% from 8.4% in 1QCY22.

Performance Non-markup expenses rose by 32% YoY, reaching PKR 22.6bln (CY21: PKR 17.1bln), driven by inflation, branch expansion, compensation, and property expenses. The Bank's before-tax profit improved by 28% to PKR 27.6bln (CY21: PKR 21.5bln). After-tax profit increased by 6% to PKR 14.2bln (CY21: PKR 13.4bln). Notably, the Bank achieved a significant 58% growth in after-tax profit, amounting to PKR 5.7bln in 1QCY23 (1QCY22: PKR 3.6bln).

Sustainability HMBL's unwavering focus on shareholder protection and customer-centric value is fortified by technologically advanced financial products. In CY22, HMBL expanded its presence by adding 41 branches, reaching a total of 500 branches across 194 cities in Pakistan.

Financial Risk

Credit Risk Net advances of the Bank constitute 31% of the total assets at end-Dec22 – increasing 32% from last year (CY22: PKR 434bln, CY21: PKR 402bln). There was an increase in the concentration of the top 20 advances at end-Dec'22, surging to 40.4% from 37% at end-Dec'21. During 1QCY23, the advances increased by 1.1% to report PKR 439bln. Non-performing loans of the Bank reflected an increase and were reported at PKR 21.6bln (CY21: PKR 16.8bln). The infection ratio has impaired to 4.8% as compared to 4% in CY21.

Market Risk The investment portfolio reflected a growth of 8.5% to PKR 708bln during CY22 (CY21: PKR 652bln). The bank's investment portfolio constitutes 50.6% of the total asset base and government securities continue to dominate the overall investment book (99.2%). The total investment in PIBs in CY22 was registered at PKR 396.5bln, and the bank incurred unrealized losses on PIBs in CY22, due to interest rate movement, which increased in 1QCY23. The investment portfolio witnessed a further expansion during 1QCY23 to report at PKR 772bln.

Liquidity And Funding Deposits were reported at PKR 880bln as against PKR 772bln last year. At the year-end, the ADR stands at 49%. ADR further dropped to 47% as at end-Mar23. Further, the bank's CASA remained largely the same YoY at 63.9%.

Capitalization Bank's CAR as at end-Dec22 is 14.6% (CY21: 14.1%), and as of Mar'23, it is 14% against the regulatory requirement of 11.50%. The equity base of the bank displayed a growth trajectory over the last few years; augmented to PKR ~74.5bln as at end-Dec'22 (end-Dec21: PKR 62bln).

PKR mln

Habib Metropolitan Bank Limited Listed Public Limited	Mar-23 3M	Dec-22 12M	Dec-21 12M	Dec-20 12M
A BALANCE SHEET				
1 Total Finances - net	456,492	449,492	418,541	325,951
2 Investments	772,449	707,809	651,946	570,761
3 Other Earning Assets	24,205	82,529	19,529	16,488
4 Non-Earning Assets	178,445	157,833	138,510	104,386
5 Non-Performing Finances-net	417	(219)	(4,109)	(14)
Total Assets	1,432,008	1,397,444	1,224,417	1,017,572
6 Deposits	936,112	880,697	772,286	680,956
7 Borrowings	309,949	343,968	316,167	201,723
8 Other Liabilities (Non-Interest Bearing)	112,727	98,272	72,989	77,245
Total Liabilities	1,358,788	1,322,937	1,161,442	959,924
Equity	73,220	74,507	62,975	57,648
B INCOME STATEMENT				
1 Mark Up Earned	44,193	133,165	73,396	76,123
2 Mark Up Expensed	(30,423)	(92,554)	(43,899)	(47,361)
3 Non Mark Up Income	3,964	13,215	11,140	9,650
Total Income	17,735	53,826	40,637	38,413
4 Non-Mark Up Expenses	(6,625)	(22,677)	(17,087)	(14,875)
5 Provisions/Write offs/Reversals	(1,045)	(3,531)	(2,009)	(3,502)
Pre-Tax Profit	10,065	27,617	21,541	20,037
6 Taxes	(4,340)	(13,357)	(8,082)	(8,029)
Profit After Tax	5,725	14,261	13,459	12,008
C RATIO ANALYSIS				
1 Performance				
Net Mark Up Income / Avg. Assets	3.9%	3.1%	2.6%	3.1%
Non-Mark Up Expenses / Total Income	37.4%	42.1%	42.0%	38.7%
ROE	31.0%	20.7%	22.3%	23.6%
2 Capital Adequacy				
Equity / Total Assets (D+E+F)	5.1%	5.3%	5.1%	5.7%
Capital Adequacy Ratio	14.0%	14.6%	14.1%	16.8%
3 Funding & Liquidity				
Liquid Assets / (Deposits + Borrowings Net of Repo)	65.5%	57.1%	61.2%	67.6%
(Advances + Net Non-Performing Advances) / Deposits	47.0%	49.2%	51.6%	45.8%
CA Deposits / Deposits	37.6%	34.8%	34.7%	32.4%
SA Deposits / Deposits	30.1%	29.1%	28.6%	27.9%
4 Credit Risk				
Non-Performing Advances / Gross Advances	5.0%	4.8%	4.0%	5.8%
Non-Performing Finances-net / Equity	0.6%	-0.3%	-6.5%	0.0%

Credit Rating

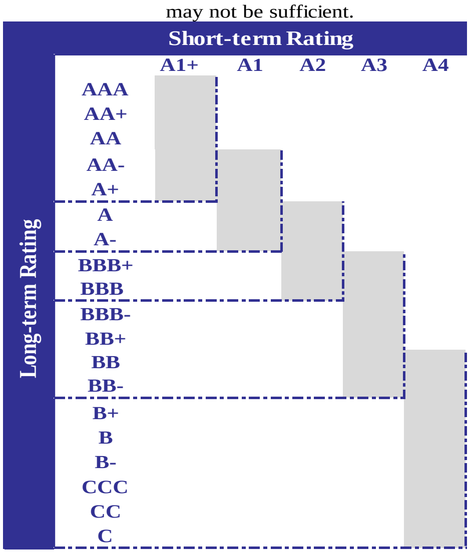
Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

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

Regulatory and Supplementary Disclosure

(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

Restrictions

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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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