The Pakistan Credit Rating Agency Limited

Rating Report

MCB Bank Limited

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
23-Jun-2022	AAA	A1+	Stable	Maintain	-
23-Jun-2021	AAA	A1+	Stable	Maintain	-
26-Jun-2020	AAA	A1+	Stable	Maintain	-
27-Dec-2019	AAA	A1+	Stable	Maintain	-
27-Jun-2019	AAA	A1+	Stable	Maintain	-
27-Dec-2018	AAA	A1+	Stable	Maintain	-
27-Jun-2018	AAA	A1+	Stable	Maintain	-
29-Dec-2017	AAA	A1+	Stable	Maintain	-
19-Jun-2017	AAA	A1+	Stable	Maintain	-
24-Jun-2016	AAA	A1+	Stable	Maintain	-

Rating Rationale and Key Rating Drivers

The ratings take comfort from MCB's sustained market and financial position. This has been enabled by the bank's able parentage, wherein a diverse mix of sponsors - mainly led by Nishat Group - have been providing an effective oversight. The rating factors in MCB's strong market positioning, supported by its well-established brand name and substantial out-reach. MCB retained its position as the player with highest CASA in the banking industry. A slowdown was witnessed in the growth pace of the bank. The large bank’s universe is seeing major challenge due to some banks which have lately recorded massive growth. Holding onto its respective share is important. There has been a change at the helm of affairs, which it is hoped would provide impetus to the growth proposition. The bank continues with its current strategy of lending to premier corporates along with key focus on government securities. From risk perspective, it is favorable, especially when it is supplemented by a sizeable investment book, reaching a trillion-rupee mark. The bank remained focused on taking a cautious yet balanced approach with respect to its advance’s portfolio. The advances book witnessed significant increase, during CY21, improving ADR of the bank. MCB has marked its position as the bank with notable profit base since the last few years. The bank has established an Islamic Banking subsidiary, thereby, becoming the first conventional bank to do so. Pakistan’s economy has gone through several varied phases in last two years due to the COVID19 pandemic. Banking sector continued to flourish with high profitability. Going forward, the macro-economic environment is beset with myriad challenges due to heightened interest rate, tightening of demand, rupee depreciation and higher inflation. This has repercussions for all segments of the economy.

The ratings are dependent on the bank's ability to hold its existing position in the banking sector. Any deterioration in the perceived strength of the bank or ownership with consequent impact upon its governance efficacy would have negative implication. CAR of the Bank as on Mar-22 reported at 16.35% (CY21: 17.01%).

Disclosure

Name of Rated Entity	MCB Bank Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology | Financial Institution Rating(Jun-21),Criteria | Correlation Between Long-term & Short-term Rating Scales(Jun-21),Criteria | Rating Modifiers(Jun-21)
Related Research	Sector Study | Commercial Bank(Jun-22)
Rating Analysts	Sehar Fatima | sehar.fatima@pacra.com | +92-42-35869504

Profile

Structure MCB Bank Limited (hereinafter referred as “MCB” or “the bank”) was incorporated as a public limited company, in 1947, and is listed on Pakistan Stock Exchange (PSX).

Background Bank commenced operations in 1947 and was privatized in 1991.

Operations MCB offers a wide range of products and services hence ensuring ease and freedom for the customer to bank from any of the 1,426 branches as of Mar'22 (as at YE-Dec,21: 1,426) across the country and a wide array of digital channels.

Ownership

Ownership Structure MCB Bank is substantially owned by Nishat group, through (direct and indirect holdings) individuals of Mansha family and corporates of the group.

Stability The ownership of the bank is expected to stay stable in the foreseeable future as the bank is one of the flagship entities of Nishat Group.

Business Acumen Nishat Group, including individual holdings and holding through group corporates, is a premier business house of Pakistan and is one of the leading and most diversified in South East Asia, having presence in Textile, Cement, Insurance, Banking, Financial Services, Power Generation, Hotel & Hospitality, Dairy, Paper Products, Retail Commerce, Real Estate, Agriculture, Aviation and Automotive sectors.

Financial Strength Nishat group is one of the leading and most diversified in South East Asia. The group has a strong equity and asset base.

Governance

Board Structure MCB encourages representation of independent directors, non-executive directors and directors representing minority interests on its board of directors. At present, apart from CEO, the Board includes four independent directors and eight non-executive directors. All the directors on the Board are non-executive except for the CEO of the Bank. The non executive directors provide an independent oversight to the Board.

Members’ Profile Mian Mohammad Mansha is the Chairman of the Board. Mr. Shoaib Mumtaz is the President and CEO of the Bank. Effective from December 21, 2021, he has been appointed by the board after completion of term of Mr. Imran Maqbool.

Board Effectiveness The board with its active engagement with the stakeholders is well poised to govern the bank and oversee implementation of its strategy. To ensure effective and independent oversight of the bank’s overall operations, the Bank has eight board committees.

Financial Transparency The external auditors of the bank, A. F. Ferguson & Co., Chartered Accountants, issued an unqualified audit opinion pertaining to annual financial statements for CY21. Furthermore, the Board has set up an effective internal audit function that reports independently to the Audit Committee.

Management

Organizational Structure MCB has a lean organizational structure that clearly defines responsibilities, authority and reporting lines with proper monitoring and compliance mechanism. The bank, with a largely horizontal organizational structure, has multiple groups & divisions reporting to the CEO, except Internal Audit and Corporate Affairs that reports to the Board’s Audit Committee and the Board respectively.

Management Team Mr. Shoaib Mumtaz - President and CEO - business graduate from the United States, is a seasoned banker with almost three decades of experience with MCB. He has served at various key positions in Branch Banking, Credit Risk, Corporate Finance and International Banking. MCB’s senior management team comprises experienced bankers having national and international exposure.

Effectiveness The Bank has sixteen management committees in place each with defined terms of reference. Comprising of senior officials including the President, meetings are held on a regular basis and agenda items include developing business plans.

MIS MCB management has centralized the authority, direction, management, and monitoring of Information Security activities for the entire organization in the Information Technology Group (ITG) under the umbrella of Information Security (IS) Team. ITG is headed by CIO who in turn reports functionally and administratively to the CEO.

Risk Management Framework Prudent risk management aspects are embedded in the bank’s strategy, organizational structure, processes, and systems and controls. Risk Management & Portfolio Review Committee remains responsible to ensure that appropriate risk management policies are developed and implemented to mitigate the key risks to which the bank is exposed.

Business Risk

Industry Dynamics Pakistan’s economy has gone through several varied phases in last two years. The economic activity revived 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). 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%).

Relative Position MCB retained its position among top-5 banks in terms of customer deposits market share. As at end-Dec21, the absolute value of the customer deposit stands at PKR ~1.4tln (end-Dec20: PKR ~1.3tln).

Revenues During CY21, net markup earned declined to PKR 64.0bln (CY20: PKR 71.3bln). This is attributable to decrease in markup earned to PKR 123.3bln (CY20: PKR 136.1bln) – mix tilted towards income from investments (CY21: PKR 89.5bln, CY20: PKR 92.0bln) – primarily due to low key policy rate prevailing during last year. During 1QCY22, the Bank earned net markup income of PKR 18.1bln (1QCY21: PKR 15.2bln), reflecting an increase of 19%.

Performance Non-markup income block of the Bank was reported at PKR 20.0bln (CY20: PKR 18.1bln) with major contributions coming in from fee and commission income (CY21: PKR 12.4bln, CY20: PKR 10.9bln). Non-mark-up income to total income ratio increased to 23.9% (CY20: 20.3%). During CY21, net profitability (PAT) of the Bank (increased by 6%) and was reported at PKR 30.8bln (CY20: PKR 29.0bln). During 1QCY22, total income recorded good improvement to PKR 23.8bln (1QCY21: PKR 20.0bln). Net profitability clocked in at PKR 8.9bln (1QCY21: PKR 6.7bln); up 31%.

Sustainability Going forward, the bank’s strategy will hover around increase in current deposits, improvement in asset quality, development of human capital, expansion in branch network and enhancement of digital infrastructure.

Financial Risk

Credit Risk Credit risk review ensures to minimize credit risk associated at account and portfolio level. Total finances of the Bank constitute 28.4% of the total assets as at end-Dec21. Gross performing advances increased by 26.6% to PKR 585bln (as at end Dec-20: PKR 462bln). During 1QCY22, gross performing advances declined slightly to clock in at PKR 579mln. At end-Dec21, non-performing loan base of the Bank slightly declined to report at PKR 50.5bln (end-Dec20: PKR 51.2bln). Hence, infection was reported at 7.9% (end-Dec20: 10.0%).

Market Risk MCB is exposed to market risk primarily through its trading activities, which are centered in the Treasury and Foreign Exchange Group and the Capital Market Division. The investment portfolio reflected uptick of 2% as it stood at PKR 1,026.5bln during CY21 (end-Dec20: PKR 1,005bln). The bank’s investment portfolio constitutes 50.3% of total asset base whereas government securities continue to dominate the overall investment book (~96%).

Liquidity And Funding MCB’s liquidity risk management framework is designed to identify, measure and manage in a timely manner the liquidity risk position of the Bank. During CY21, the deposit base of the bank increased by 9.3%, clocking in at PKR 1,412bln (CY20: PKR 1,289.5bln). The Bank reported a high CASA ratio of ~91% in CY21.

Capitalization Banks’s total CAR reported at 17% (has been above the regulatory requirement of 11.5%) - including capital conservation buffer of 2.5%. Quality of the capital is evident from Bank’s Common Equity Tier-1 (CET-1) to total risk weighted assets ratio which comes to 15.1% against the requirement of 6%.

PKR mln

MCB Listed Public Limited	Mar-22 3M	Dec-21 12M	Dec-20 12M	Dec-19 12M
A BALANCE SHEET				
1 Total Finances - net	589,666	594,211	472,941	501,254
2 Investments	1,167,864	1,026,458	1,005,289	738,124
3 Other Earning Assets	63,870	63,353	29,587	19,259
4 Non-Earning Assets	267,726	281,818	249,064	250,449
5 Non-Performing Finances-net	6,205	4,628	581	6,066
Total Assets	2,095,331	1,970,468	1,757,462	1,515,152
6 Deposits	1,491,685	1,411,852	1,289,502	1,144,763
7 Borrowings	320,641	269,526	164,002	89,506
8 Other Liabilities (Non-Interest Bearing)	110,046	114,684	113,857	111,968
Total Liabilities	1,922,372	1,796,061	1,567,361	1,346,237
Equity	172,959	174,407	190,102	168,915
B INCOME STATEMENT				
1 Mark Up Earned	39,717	123,334	136,076	138,292
2 Mark Up Expensed	(21,605)	(59,347)	(64,741)	(78,676)
3 Non Mark Up Income	5,722	20,074	18,136	16,679
Total Income	23,834	84,061	89,470	76,295
4 Non-Mark Up Expenses	(9,769)	(36,894)	(33,908)	(33,709)
5 Provisions/Write offs/Reversals	863	4,823	(7,313)	(2,484)
Pre-Tax Profit	14,928	51,989	48,249	40,102
6 Taxes	(6,014)	(21,178)	(19,212)	(16,125)
Profit After Tax	8,914	30,811	29,037	23,977
C RATIO ANALYSIS				
1 Performance				
Net Mark Up Income / Avg. Assets	3.6%	3.4%	4.4%	4.0%
Non-Mark Up Expenses / Total Income	41.0%	43.9%	37.9%	44.2%
ROE	20.5%	16.9%	16.2%	15.1%
2 Capital Adequacy				
Equity / Total Assets (D+E+F)	8.3%	8.9%	10.8%	11.1%
Capital Adequacy Ratio	16.3%	17.0%	21.0%	18.9%
3 Funding & Liquidity				
Liquid Assets / (Deposits + Borrowings Net of Repo)	70.1%	69.0%	76.9%	69.8%
(Advances + Net Non-Performing Advances) / Deposits	39.2%	41.8%	35.9%	43.4%
CA Deposits / Deposits	39.5%	37.8%	35.9%	34.9%
SA Deposits / Deposits	50.0%	53.0%	55.0%	53.3%
4 Credit Risk				
Non-Performing Advances / Gross Advances	8.1%	7.9%	10.0%	9.2%
Non-Performing Finances-net / Equity	3.6%	2.7%	0.3%	3.6%

Credit Rating

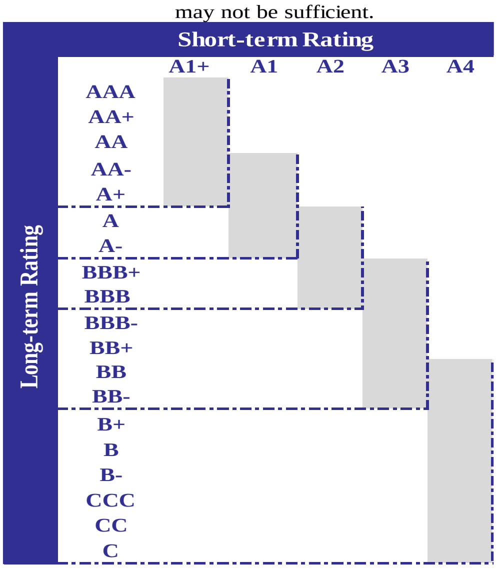
Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

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

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
(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