



The Pakistan Credit Rating Agency Limited

Rating Report

MCB Bank Limited

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Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
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 note of MCB's sustained financial profile, reflected in very strong capitalization, sound liquidity and diverse deposit base. 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 ratings factor in MCB's strong market positioning, supported by its well established brand name and substantial out-reach. MCB has one of the highest CASA in the industry, with lowest cost of funds amongst all players. The bank has added a sizeable chunk to its deposit base. The bank continues with its current strategy of lending to premier corporates with sustained focus on government exposure. Lately, the bank has added momentum to its growth trajectory. The bank has established an Islamic Banking subsidiary, thereby, becoming the first conventional bank to do so.

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. Further strengthening of human resource would be vital.

Disclosure

Name of Rated Entity	MCB Bank Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology Financial Institution(Jun-18),Methodology Criteria Rating Modifier(Jun-18),Methodology Correlation Between Long-Term And Short-Term Rating Scale(Jun-18)
Related Research	Sector Study Commercial Bank(Jun-18)
Rating Analysts	Muhammad Obaid muhammad.obaid@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. In 2017, Bank expanded its retail footprint in the form of merger of NIB Bank with and into MCB and with effect from June 2018, MCB transferred 90 branches to MCB Islamic Bank along with deposits of ~22 bln.

Operations MCB offers a wide range of products and services hence ensuring ease and freedom for the customer to bank from any of the 1350+ branches across the country and a wide array of digital channels.

Ownership

Ownership Structure The bank is majority owned (~36%) by Nishat group, through individuals of Mansha family and corporates of the group, and Maybank (~19%).

Stability Development and retention of high potential employees so as to create a talent pool from which to fill key positions in the organization. This is a continuous process, which in turn ensures that the organization’s management is able to keep up with the changing business environment.

Business Acumen Mansha Group, including individual holdings and holding through group corporates, is a premier business house of Pakistan, having presence in the Textile, Cement, Insurance, Banking, Power Generation, Hotel & Hospitality, Real Estate and other sectors. It operates in various countries across the globe including Sri Lanka, Azerbaijan, UAE and Bahrain.

Financial Strength Mansha group is one of the leading and most diversified in South East Asia. The group has a strong equity and asset base. Further Maybank, holding 19%, stake in MCB, is the largest financial services group in Malaysia.

Governance

Board Structure The ten member board is headed by Mr. Mian M Mansha. President / CEO Mr. Imran Maqbool is the only executive director, while the remaining are non-executive directors including two representatives of Maybank.

Members’ Profile Chairman of the board, Mr. Mian M Mansha, is a well-known and seasoned businessperson with over 45 years experience. He was presented with Pakistan’s Civil Award for his contributions to industrial development, in 2004. Further, he is accompanied by members with diversified experience and quality education.

Board Effectiveness The board with its active engagement with the stakeholders is well poised to govern the bank and oversee implementation of its strategy. The BoD has constituted eight board committees to ensure rigorous monitoring of the management’s policies and bank’s operations.

Financial Transparency M/s. KPMG Taseer Hadi, Chartered Accountants, expressed an unmodified conclusion vide their review report for half year ended Jun18. Further, an Internal Audit function is in place that provides critical assurance to the Board and management in assessing overall strength of the bank’s control environment.

Management

Organizational Structure MCB’s organizational structure having appropriate resources and systems within the Bank, ensures that the Senior Management focuses on key functions and executes strategies timely and effectively.

Management Team MCB’s senior management team comprises experienced bankers having national and international exposure. Mr. Imran Maqbool, CEO, is a seasoned banker with over three decades of diverse, international banking experience. Before joining MCB in 2002, he was associated with Bank of America and Citi Bank where he worked at senior management roles.

Effectiveness Bank has fourteen management committees in place each with defined terms of reference to ensure smooth execution of business strategy. Comprising of senior officials including the President, meetings are held on a regular basis and agenda items include developing business plans, reviewing the performance of the Bank on standalone basis as well as compared to the sector.

MIS Management of the Bank has centralized the authority, direction, management, and monitoring of Information Security activities.

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 The banking industry witnessed significant expansion in the loan book. Last year and YTD (2018) both witnessed huge deployments. This is expected to slow down. New projects require gestation period and additionally crowding-out effect may take place. Rising interest rates mean profitability of the sector would take support. Yet NPLs, as a result, may also transpire. CAR is reaching the maximum requirement by December 2018 (11.9%). This will create a challenge for some of the players.

Relative Position Bank’s customer deposits (PKR 1,007 bln) increased by ~6.3% inline with the sector’s growth of 6%. MCB retained its position in top 5 banks on the basis of advances, deposits and profitability with share in total deposits of the sector at 8% (Dec17: 8%).

Revenues Net interest revenue for the nine months witnessed an increase of ~7.8% YoY and stands at PKR 33.9 bln on account of strategic measurement of earning asset mix. Non-markup income reflected a decrease of ~15% YoY, primarily on account of dismal capital market performance as evident from ~32% decrease in dividend income.

Performance ROE of the Bank decreased 370 bps from 17.7% in Dec17 to 14.0% in Sep18, significant decrease was on account tax provision reversal of PKR 3.6 bln recorded in 2017 and increased administrative expenses (23% YoY) mainly associated with Ex-NIB operational activity. On provisions against advances front, Bank continued with its recovery trajectory and posted a reversal of PKR 1.9 bln.

Sustainability A number of product initiatives have been taken which will be beneficial for bank’s growth and going forward more initiatives are in pipeline to provide Customers financial solutions and security.

Financial Risk

Credit Risk To ensure a prudent distribution of asset portfolio, the Bank manages its lending and investment activities within an appropriate limits framework. Non-performing loan base of the Bank reduced by PKR 1.7 bln in nine months on account of recoveries made or settlements executed during the period. Coverage and Infection ratios stand at 93.3% (Dec17: 93.7%) and 8.9% (Dec17: 9.5%) respectively.

Market Risk Market risk, in terms of MCB’s exposure of investment book, now representing 41% of total earning assets as at Sep18, witnessed a dip from 57% at Dec17. Investments continued to remain concentrated in government securities (Sep18: 89%; Dec17: 93%).

Liquidity And Funding Total customer deposit base of the Bank registered a significant increase of ~PKR 60bln (6%) which resulted in the Bank crossing One Trillion Deposit benchmark. Further, the portion of CASA stands at 92.3% at Sep18 and Advances-to-deposits ratio decreased slightly to 47.2% at Sep18 (Dec17: 48.5%).

Capitalization Bank remains adequately capitalized, with CAR for Sep18, reported at 15.21% (Dec17: 16.44%). The Bank’s Liquidity Coverage Ratio (LCR) at September 18 is 177%, while the Bank’s Net Stable Funding Ratio (NSFR) as at Sep 18 is 130%, which are both well in excess of SBP prescribed minimum requirement.



MCB Bank Limited

BALANCE SHEET	30-Sep-18	31-Dec-17	31-Dec-16	31-Dec-15
	9M	Annual	Annual	Annual
Earning Assets				
Advances (Net of NPLs)	484,325	466,305	346,126	312,258
Debt Instruments	10,776	7,797	5,899	9,927
Total Finances	495,101	474,102	352,025	322,185
Investments	443,414	649,166	550,030	558,875
Others	155,159	15,507	10,063	12,651
	1,093,674	1,138,776	912,118	893,711
Non Earning Assets				
Non-Earning Cash	123,873	99,542	71,313	57,372
Deferred Tax	-	-	-	-
Net Non-Performing Finances	3,175	3,051	1,990	1,867
Fixed Assets & Others	75,254	85,942	66,393	63,679
	202,302	188,535	139,696	122,918
TOTAL ASSETS	1,295,976	1,327,311	1,051,814	1,016,630
Interest Bearing Liabilities				
Deposits	1,032,649	968,483	781,430	708,091
Borrowings	59,729	136,962	74,515	118,459
	1,092,378	1,105,445	855,945	826,551
Non Interest Bearing Liabilities	54,955	68,300	54,242	52,279
TOTAL LIABILITIES	1,147,333	1,173,745	910,187	878,829
EQUITY (including revaluation surplus)	148,643	153,566	141,627	137,800
Total Liabilities & Equity	1,295,976	1,327,311	1,051,814	1,016,630
INCOME STATEMENT	30-Sep-18	31-Dec-17	31-Dec-16	31-Dec-15
	9M	Annual	Annual	Annual
Interest / Mark up Earned	58,926	74,091	67,422	80,532
Interest / Mark up Expensed	(25,016)	(31,684)	(23,655)	(31,210)
Net Interest / Markup revenue	33,910	42,407	43,767	49,322
Other Operating Income	10,843	17,339	15,901	16,705
Total Revenue	44,753	59,746	59,668	66,027
Other Income / (Loss)	914	621	320	410
Non-Interest / Non-Mark up Expensed	(24,488)	(28,679)	(23,260)	(23,560)
Pre-provision operating profit	21,179	31,688	36,728	42,877
Provisions	2,136	(673)	(654)	(544)
Pre-tax profit	23,315	31,014	36,075	42,333
Taxes	(9,004)	(8,555)	(14,184)	(16,782)
Net Income	14,311	22,459	21,891	25,550
RATIO ANALYSIS	30-Sep-18	31-Dec-17	31-Dec-16	31-Dec-15
	9M	Annual	Annual	Annual
Performance				
ROE	14.0% *	17.7%	19.0%	23.2%
Cost-to-Total Net Revenue	54.7%	48.0%	39.0%	35.7%
Provision Expense / Pre Provision Profit	-10.1%	2.1%	1.8%	1.3%
Equity/Total Assets	10.5%	10.3%	11.2%	11.1%
Funding & Liquidity				
Liquid Assets / Deposits and Borrowings	66.3%	66.1%	73.1%	74.9%
Advances / Deposits	47.2%	48.5%	44.5%	44.4%
CASA deposits / Total Customer Deposits	92.3%	92.9%	94.1%	92.9%
Intermediation Efficiency				
Asset Yield	7.2% *	7.4%	7.7%	9.6%
Cost of Funds	3.0% *	3.2%	2.8%	4.0%
Spread	4.1% *	4.1%	4.9%	5.7%
Outreach				
Branches	1,367	1,444	1,238	1,246

*annualized

December 2018

Credit Rating Scale & Definitions

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 Ratings		Short Term Ratings	
AAA	Highest credit quality. Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments	A1+	The highest capacity for timely repayment.
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.	A1	A strong capacity for timely repayment.
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.	A2	A satisfactory capacity for timely repayment. This may be susceptible to adverse changes in business, economic, or financial 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.	A3	An adequate capacity for timely repayment. Such capacity is susceptible to adverse changes in business, economic, or financial conditions.
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	The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions.
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.	C	An inadequate capacity to ensure timely repayment.
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.		



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, a) some material identifiable event and/or b) deviation from expected trend. 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 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) cessation of underlying entity, c) the debt instrument is redeemed, d) the rating remains suspended for six months, e) the entity/issuer defaults, or/and f) PACRA finds it impractical to surveil the opinion due to lack of requisite information.

Harmonization A change in rating due to revision in applicable methodology or underlying scale.

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(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.
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- (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)

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- (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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