



The Pakistan Credit Rating Agency Limited

Rating Report

National Bank of Pakistan

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Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
28-Dec-2018	AAA	A1+	Stable	Maintain	YES
30-Jun-2018	AAA	A1+	Stable	Maintain	-
30-Dec-2017	AAA	A1+	Stable	Maintain	-
23-Jun-2017	AAA	A1+	Stable	Maintain	-
30-Jun-2016	AAA	A1+	Stable	Maintain	-

Rating Rationale and Key Rating Drivers

The ratings are driven by strong ownership structure (Government of Pakistan (GoP) holds majority stake). The bank's strong financial risk profile, characterized by firm risk absorption capacity, provides strength to the ratings. NBP's renowned franchise along with extended outreach aids the bank in deposit mobilization; public-private deposit mix remained intact. NBP fortified its position as the second largest bank in the country in terms of customer deposits. During 9MCY18, the bank's deposit base saw a massive expansion. Additionally CASA mix improved; optimizing cost of funding. High admin cost of the bank is limiting profitability. There was deterioration in the asset quality as NBP booked PKR 15bln of NPLs. The management is confident as to recoveries. Overseas operations (forex) and domestic private credit are contributors to fresh infection. Going forward, the bank is keen to strengthen its lending portfolio; entering into profitable avenues seems a challenge. With focused efforts, NBP has managed to bring volumes in Islamic banking (Aitemaad) though limited; it is targeted to contribute towards growth.

The ratings are dependent upon the management's ability maintain relative standing of the bank in the industry in all key parameters. Banks (Nationalization) Act, 1974 (clause 4 of section 5) provides for the safety of all deposits in the banks. Depositor Protection Act 2016 (clause 39) has removed the protection clauses of the referred Act. Which law is to prevail, should any dispute arise, is a legal matter. Moreover, the bank in a case related to pensioner benefits to retired employees has filed a review petition against the Supreme Court judgment and has also moved an application for constitution of larger bench which has been accepted.

Disclosure

Name of Rated Entity	National Bank of Pakistan
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 National Bank of Pakistan (NBP) was incorporated in Pakistan was incorporated under National Bank of Pakistan Ordinance, 1949 and is listed on the Pakistan Stock Exchange.

Background NBP is engaged in providing commercial banking and related services in Pakistan and overseas. NBP is authorized to act as agent of State Bank of Pakistan (SBP) and handles treasury operations for Government of Pakistan (GoP).

Operations The Bank, with its head office in Karachi, operates with a network of 1502 branches in Pakistan and 21 overseas branches as at end-Sep18.

Ownership

Ownership Structure NBP is majorly owned (75.6%) by the Government of Pakistan (GoP), mainly through the SBP (75.2%). The remaining stake is spread among financial institutions, and general public.

Stability Being the largest public sector commercial bank, NBP is of strategic importance to the GoP. An implicit guarantee is provided against liabilities (deposits) of NBP under The Bank's (Nationalization) Act, 1974.

Business Acumen SBP, which has a major stake in NBP on behalf of GoP, stands to provide it with the industry-specific working knowledge and strategic thinking capability as it has a holistic view of the entire industry.

Financial Strength The GoP has provided assistance to the Bank in the past and shall continue to support it as implicit guarantee is provided against liabilities (deposits) of NBP under The Bank's (Nationalization) Act, 1974.

Governance

Board Structure According to BNA, 1974, the bank is required to have a minimum of six members BoD at any point in time. GoP nominated seven-member board of directors including the President & CEO; one executive, six non-executive including one independent director.

Members' Profile The board carries diversified experience including financial sector, particularly banking, civil services, and other businesses. Most of the directors have above two decades of experience.

Board Effectiveness During the year, 8 board meetings (CY17: 10) were held; attendance of directors remained high. Relatively, large number of meetings reflects continuous monitoring of affairs pertaining to oversee operations. High attendance of members reflects active oversight.

Financial Transparency The Audit & Compliance Committee reports directly to the board. The committee comprises six members, all of whom are non-executive directors while four of them are independent directors including the chairman. This ensures effective, transparent and independent oversight. The bank has joint external auditors; Ernst and young Ford Rhodes Sidat Hyder Chartered accountants and Grant Thornton Anjum Rahman Chartered accountants. Joint auditors expressed an unqualified opinion on the bank's financial statements for the year ended December 31, 2017.

Management

Organizational Structure NBP has divided its functions into 19 departments, each of which reports directly to President, except the Audit and Inspection Group, which reports to Board Audit & Compliance Committee.

Management Team NBP's senior management team comprises experienced bankers. Mr. Tariq Jamali, President and CEO, who joined NBP in 1987 is a seasoned banker having over three decades of experience of domestic and international markets.

Effectiveness NBP has an effective mix of management committees which are established to monitor performance and assure the adherence to the policies and procedures.

MIS NBP uses "Profile" as its core banking application (CBA). The Bank is using MisysKondor for Treasury function while, SAP is used for Financial General Ledger and Human Resources Management. The bank has established a new division – Payment Services and Digital Banking Group. This is in line with management's strategy of adopting digitization.

Risk Management Framework NBP's risk management framework resides with Risk Management Group (RMG). RMG develops risk management policies and tools in line with SBP guidelines while ensuring implementation by respective departments. RMG has 7 wings to help manage the different facets of risk profile of the Bank.

Business Risk

Industry Dynamics Pakistan's economy is at an important juncture, whereby the need of the hour is timely materialization of financial inflows and continued reduction in the import bill. For the 9MCY18 the banking sector experienced a slower growth of 6% in its deposit base (CY17: 10%) due to slowing economy. Pressure will abate from CAR as profitability would increase amidst maturing PIBs. With the increasing interest rate environment, new governments mission to build 5 million houses, and facilitating export oriented manufacturing concerns bodes well for the Banking Industry.

Relative Position NBP, a large sized bank, holds a good position in the industry with a 12.6% customer deposit base of PKR 1,585bln at end-Sep18.

Revenues For the 9MCY18, the bank's interest revenue witnessed an increase of ~14% on a YoY basis to PKR 43.5bln (9MCY16: PKR 38.3bln), on the back of volumetric growth as well as rising interest rate environment. AKBL booked higher income from fee commission and brokerage by ~9% (9MCY18: PKR 12.5bln; 9MCY17: PKR 11.5bln) due to better volumes in trade related business and bancassurance sales. Increase in revenue was supported by income from dealing in foreign currencies which saw a huge jump of 1.1x (9MCY18: PKR 3.0bln; 9MCY17: PKR 1.4bln) on account of prudent FX management amid depreciating PKR. Capital gains dipped to PKR 3.2bln (9MCY17: PKR 6.2bln) as last years' significant chunk was realized gain from PIBs.

Performance For the 9MCY18, the bank's yield on advances improved with rising interest rates and stood at *7.2% compared to last years' 6.7% (*annualized). Consequently the bank's cost of deposits also increased slightly during the period (9MCY17: *4.5%, CY17: 4.2%). Higher volumetric growth coupled with improvement on the asset yield side overshadowed the higher cost of funds, bringing the spread for 9MCY18 to 2.7% (CY17: 2.5%). NIMR ratio stayed stagnant at *2.5% (CY17: 2.5%). The bank was able to keep a check on its non-markup expenses (9MCY18: PKR 38.5bln; 9MCY17: PKR 38.1bln) bringing down the cost to total net revenue on a YoY basis (9MCY18: ~60%, 9MCY17: ~63%). Although during the 9MCY18, the Bank made additional provisioning, it was still able to sustain its profitability on a YoY basis as net income clocked in at PKR 16.2bln (9MCY17: PKR 14.7bln).

Sustainability The budgeted forecasts and actual numbers of NBP have strong correlation. Increasing interest rate environment helped the bank in increasing its spread and earning higher profitability.

Financial Risk

Credit Risk During the 9MCY18, NBP's gross advances registered a growth of ~12%, mainly financed through deposits. Growth in advances was below industry average of 15%. Moreover, AKBL registered highest growth in advances portfolio vis-à-vis mid-sized peer banks. Advances-to-Deposits ratio on the back of higher credit off-take by the bank increased to 46% at end-Sep18 (end-Dec17: 43%).

Market Risk NBP's investment portfolio comprises 59% of total earning assets. At end-Sep18, investments stood at PKR ~1,247bln, registering ~4% contraction for the period on account of maturing PIBs. The investment portfolio remained dominated in government securities (~75%). Exposure in high yielding PIBs increased to 28% at end-Sep18 (CY17: ~23%). Exposure in short term govt. papers decreased during the period to 57% (CY17: 63%); as the bank changes its portfolio mix considering upward pressure on interest rates in short to medium-term.

Liquidity And Funding NBP's customer deposit base stood at PKR 1,585bln at end-Sep18, thereby registering ~9% during the year. Top-20 deposits concentration remained stagnant at 17% at end-CY17 (end-CY16: 17%); considered good. CASA mix improved by a fair margin to 82% (CY17: 77%); lower than other large banks. The liquidity of the bank measured in terms of Liquid Assets / Deposits and Borrowings decreased to 62% (CY17: 65%) which is slightly lower compared with other comparable peer banks.

Capitalization NBP's capitalization stood at 18.1% at end-Sep18 (end-Dec17: 16.0%). CAR is strong and predominantly comprises Tier-I capital (11.4%).



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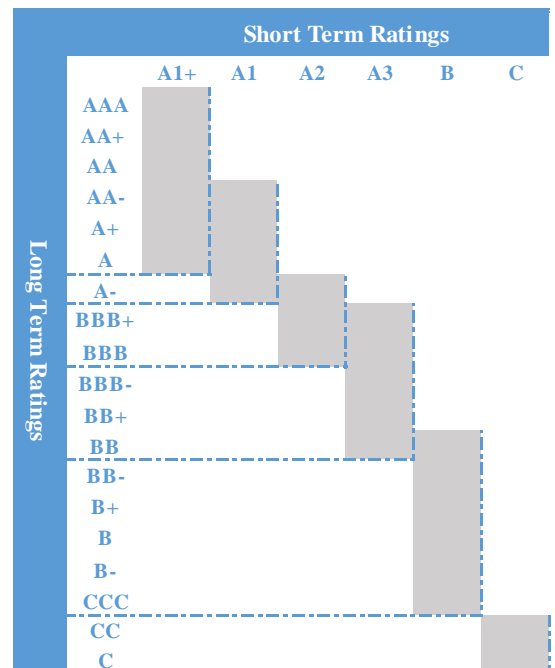
National Bank of Pakistan (NBP)

	30-Sep-18	31-Dec-17	31-Dec-16	31-Dec-15
	9M	Annual	Annual	Annual
PKR mln				
BALANCE SHEET				
Earning Assets				
Advances (Net of NPL)	817,485	736,140	662,060	564,572
Debt Instruments	61,723	54,310	56,275	20,204
Total Finances	879,208	790,451	718,335	584,776
Investments	1,191,895	1,247,759	850,742	806,287
Others	37,322	46,263	134,459	24,266
	2,108,426	2,084,473	1,703,536	1,415,328
Non Earning Assets				
Non-Earning Cash	206,200	166,822	160,915	154,457
Deferred Tax	-	7,317	5,136	9,669
Net Non-Performing Finances	4,434	(2,718)	(4,557)	16,306
Fixed Assets & Others	150,234	113,992	110,676	110,601
	360,868	285,412	272,170	291,033
TOTAL ASSETS	2,469,294	2,369,885	1,975,706	1,706,361
Interest Bearing Liabilities				
Deposits	1,799,787	1,727,102	1,657,312	1,431,037
Borrowings	360,894	360,120	44,890	21,947
	2,160,681	2,087,222	1,702,202	1,452,984
Non Interest Bearing Liabilities				
	120,305	107,281	96,771	85,026
TOTAL LIABILITIES	2,280,986	2,194,503	1,798,973	1,538,010
EQUITY (including revaluation surplus)	188,308	175,382	176,733	168,351
Total Liabilities & Equity	2,469,294	2,369,885	1,975,706	1,706,361
INCOME STATEMENT				
Interest / Mark up Earned	105,217	123,073	114,403	113,662
Interest / Mark up Expensed	(61,666)	(68,820)	(59,578)	(59,941)
Net Interest / Markup revenue	43,551	54,253	54,824	53,721
Other Income	22,492	31,066	29,967	34,983
Total Revenue	66,043	85,319	84,791	88,704
Non-Interest / Non-Mark up Expensed	(38,485)	(50,395)	(48,351)	(43,667)
Pre-provision operating profit	27,558	34,924	36,440	45,037
Provisions	(4,441)	675	701	(11,821)
Pre-tax profit	23,117	35,599	37,141	33,216
Taxes	(6,939)	(12,571)	(14,389)	(13,997)
Net Income	16,177	23,028	22,752	19,219
Ratio Analysis				
Performance				
ROE	16%	19%	19%	17%
Cost-to-Total Net Revenue	60%	60%	58%	50%
Provision Expense / Pre Provision Profit	16%	-2%	-2%	26%
Capital Adequacy				
Equity/Total Assets	6%	5%	6%	7%
Capital Adequacy Ratio as per SBP	18%	16%	17%	18%
Funding & Liquidity				
Liquid Assets / Deposits and Borrowings	62%	64%	67%	67%
Advances / Deposits	46%	43%	40%	40%
CASA deposits / Total Customer Deposits	82%	77%	69%	73%
Intermediation Efficiency				
Asset Yield	7%	7%	8%	9%
Cost of Funds	5%	4%	4%	5%
Spread	3%	2%	3%	4%
Outreach				
Branches	1,502	1,498	1,448	1,403

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.

Disclaimer: PACRA's ratings are an assessment of the credit standing of entities/issue in Pakistan. They do not take into account the potential transfer / convertibility risk that may exist for foreign currency creditors. PACRA's opinion is not a recommendation to purchase, sell or hold a security, in as much as it does not comment on the security's market price or suitability for a particular investor.

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.
- (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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