

ARIF HABIB BANK LIMITED

RATINGS (OCTOBER 2007)

ARIF HABIB BANK LIMITED (AHB)

NEW

ENTITY

Long Term	A-
Short Term	A2

FINANCIAL DATA

PKR (mln)

	30-Jun-07*	31-Dec-06
Total Assets	9,584.3	5,696.4
Equity	3,109.0	3,094.0
Net Income	15.1	94.0
Equity / Total Assets %	32.44	54.31
Net NPLs / Equity %	-	-

* Based on un-audited results for 6 months ended June 30, 2007

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ASSESSMENT

- The ratings reflect AHB's strong risk absorption capacity emanating from its robust equity base, currently higher than most of its peers. The bank's strategy encompasses: (a) capitalize on the Arif Habib group's (AHG) synergies to establish a vibrant investment banking and wealth management platform, (b) tap big ticket corporate credit benefiting from its expanded equity base, and (c) participate actively in capital market operations – a forte of AHG. Meanwhile, the bank has inducted an experienced senior management team, which is focusing on the preliminary building blocks by implementing a business plan and putting in place requisite infrastructure. This includes low cost gradual expansion of branch network, taking IT initiatives and instigating risk management systems and procedures. The success of the bank will be inevitably linked to the success of these steps.
- Currently operating with 7 branches, the bank plans to add 5 more branches by end-07 and reach a network of 70 branches by 2011. The current and projected branch network is based on centralized processing center with real-time IT capability. The bank has embarked upon taking technology-based initiatives to attract retail customers. Meanwhile, the management plans to follow a low cost structure by having a major portion of smart and small branches in total number of branches. AHB is also working on establishing unique selling points – booths – for providing easy access to customers.
- In the initial years of operations, the bank plans to establish itself based on the group's strength in corporate and wealth management and investment banking to provide a critical mass to its balance sheet and a foundation to build a franchise. The bank, in this period, is planning to participate in syndicate of large commercial loans for good credit quality corporates. For approving syndicate financing, the management follows the same risk evaluation criteria as of other loan disbursements. Afterwards, the bank plans to tap SMEs and consumer financing as well with gradual expansion in the loan book. This approach would also provide time to institutionalize better operational controls and risk management system, imperative for SMEs and consumer banking.
- Nevertheless, the degree of success in terms of the achievement of the management's strategy remains to be seen. The bank faces an uphill task in mobilizing business in the presence of larger, more established commercial banks. However, the bank would benefit from contacts of the sponsors, business to be brought in through other group companies and relationships of newly inducted senior bankers. At the same time, the bank, with its limited franchise value, would be obliged to offer some sort of financial inducement to lure clientele and attract effective human resource. This is likely to reduce margins and increase the operating costs, and combined with the continuing investment in infrastructure, is expected to constrain the bank's earning potential from core operations in the initial years. Meanwhile, capital market and investment banking operations are likely to support the bottom line.
- The bank has taken certain initiatives regarding risk management systems. These include setting up of Risk Management Division (RMD), which is now functional. Moreover, draft risk management manuals have been prepared. The treasury middle office is regularly monitoring the treasury functions while producing daily and weekly reports. At the same time, credit risk review has been established having an independent review of each loan proposal and recording the findings in the form of credit risk review sheet. Moreover, a scoring based system for internal credit rating alongwith mapping grades have been developed for rating of prospective borrowers and updating process of the existing ones. The bank has acquired and installed H-plus, core-banking software. H-plus is a proven, integrated banking application capable of generating standard and customized MIS reports and is also compliant with the BASEL II requirements.
- Subsequent to the equity injection through rights issue, the bank's equity has increased to PKR 6bln. This provides AHB an edge over smaller banks having obligation to inject additional equity every year to meet the prudential requirement. At the same time, this would provide substantial cushion and comfort – in terms of both equity / assets and CAR – to build-up its loan portfolio.

KEY RATING DRIVERS

- The ratings are dependent on the bank's ability to fully utilize its prospective strengths to build a core-banking platform while implementing its business strategy, thereby improving its relative positioning in the banking sector. At the same time, stability and cohesiveness of the core management team would also be critical. The inability of the bank to overcome its inherent constraints of limited size, outreach, franchise value, core revenue streams, and human resource in a timely manner would have negative implications for the ratings.

PROFILE

- AHB, incorporated in December 2005, commenced its commercial operations in August 2006 subsequent to merger of Rupali Bank Limited (Pakistan Branch) with and into the bank. Currently, Arif Habib Group, through its main holding company – Arif Habib Securities Limited – holds the majority shareholding – about 93% – of the bank while the other major shareholder is Rupali Bank Limited of Bangladesh. AHG has diversified into various industrial businesses including fertilizer, cement, real estate in addition to financial services, and trading sectors.
- In a short time span, the bank has developed an experienced and well-qualified senior management team. Recently, the president of the bank resigned from his office and Mr. Kamal uddin Khan was appointed as new president. Mr. Khan has more than 25 years of banking experience mostly of international origin.