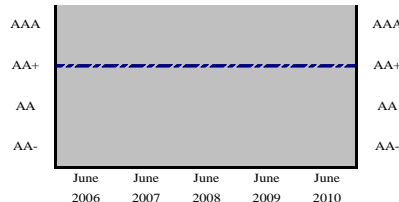


The Pakistan Credit Rating Agency Limited
RATINGS (JUNE 2010)
HABIB METROPOLITAN BANK (HMB)

	New	Previous
Entity		
Long-Term	AA+	AA+
Short-Term	A1+	A1+

LT RATING HISTORY

FINANCIAL DATA

PKR (mln)

	1Q 10*	Dec -09	Dec -08
Total Assets	237,478	237,412	182,711
Equity	18,834	18,889	16,150
Net Income	698	2,740	3,293
ROA%	1.3	1.3	1.9
ROE%	15.5	15.6	22.3
Equity/Total Assets %	7.9	8.0	8.8
Net NPLs/ equity %	12.4	9.2	-2.4
SBP CAR%	11.8	11.9	10.4

* Based on 3-months unaudited accounts for the period ended Mar 31, 2010

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RATING RATIONALE AND KEY DRIVERS

- The ratings reflect HMB's robust financial profile emanating from a strong equity base and sound liquidity position. Despite an increasingly competitive and challenging operating environment, the bank sustained its leading position in its niche market – self liquidating trade finance – while ensuring fee based income supplemented profitability. Although the bank experienced a substantial rise in NPLs, its asset quality still remains strong when compared to peers. Meanwhile, the ratings incorporate the bank's association with a geographically diversified and financially strong international bank – Habib Bank AG Zurich (HBZ).
- The management's ability to successfully execute its business strategy of diversification and growth while maintaining its market standing in its respective niche would remain critical for ratings. As the bank recently faced a significant increase in NPLs, further weakening in asset quality, in turn, putting pressure on the bank's profitability and risk absorption capacity, could have negative implications for the ratings.

ASSESSMENT

- The global financial crisis impacted the Pakistani economy with a lagged effect. Although certain macroeconomic indicators have improved, chronic power crisis, stubborn inflationary pressure, and adverse law and order situation continue to affect the overall economic activity. This is also reflected in weakening asset quality of the banks during CY09. Moreover, heavy government borrowing for budgetary support, high cost of funds, and the banking sector's cautious approach kept private sector credit off-take limited. The pace of accumulation of NPLs has stalled lately but it would be challenging for the banks to maintain asset quality amidst uncertainties regarding the recovery prospects and subdued business sentiments.
- HMB, a medium- size bank (10th largest bank in Pakistan in terms of total assets), registered modest decline in advances (6%) attributable to the management's conservative stance. However, with continued thrust for deposit mobilization, the bank's finances-to-deposit ratio benefited. HMB's interest revenue registered a healthy growth (25%), on the back of higher earning asset base and enhanced asset yield. The bank improved its spread, though still one of the lowest among peers due to large export finance portfolio. Although the profitability of the bank was impacted by higher provisioning expense (CY09: PKR 2,503mln, CY08: PKR 1,005mln), other operating income remained strong and fortified the bottom-line. The bank continued these performance trends during 1Q10.
- Historically, HMB has maintained a robust asset quality. However, it deteriorated during the year as the NPLs mounted to (2009: PKR 6,364mln; 2008: PKR 1,748mln) around 6% of total finances (CY08: 1.6%). Although it is still lower than most of the peers, managing NPLs would remain a challenge for the management. Advances to the corporate/ commercial sector (80%) represent majority of the bank's portfolio followed by SME (9%) and others. The client concentration is relatively high, with top twenty exposures representing around 32% of the total loan book. This risk is mitigated to a certain extent, based on established relationship and track record of the borrowers. The bank has a relatively high, albeit diversified, exposure to the textile sector (CY09: 53%) and relies on its cautious credit appraisal process, regular monitoring, and strong collateral to manage the associated risk.
- During 2009, the deposit base of bank grew modestly (11%), while the deposit mix changed, with a marginal increase in current and saving deposits replacing some of the high cost time deposits. Moreover, the deposit base is moderately concentrated with top 20 depositors constituting around 20% of total deposits, signifying a large diversified depositor base and strong brand recognition. Meanwhile, the investment portfolio doubled in size (CY09: PKR 97,284, CY08: PKR 48,368) during the year. In the absence of viable financing opportunities and due to the current market dynamics, the management reverted to high liquidity position with major investment in government securities (91%).
- Going forward, the management would emphasis on curtailment of the rising NPLs trend, while expanding its branch network to attract CASA deposits as well as focusing on new product development to facilitate the existing customers needs. Furthermore, HMB plans to expand its Islamic banking operations. The management is also working towards program based lending and is streamlining various risk management processes and controls. In this regard, certain functions would be centralized for effective control without greatly comprising efficiency. The pace, organization wise acceptability, and effectiveness of these initiatives remain critical for the bank.
- The bank's core operating software hPlus, provided by Bilogic System Inc., is an integrated banking solution and has been consistently upgraded to meet the growing banking requirements. HMB has finalized automatic reports for calculating CAR as per Basel requirements directly from this software.
- HMB is well capitalized and its equity-to-total assets ratio is one of the highest amongst peers. The bank's CAR improved (CY09: 11.87%; CY08: 10.42%) during the year mainly due to higher proportion of risk free assets. HMB's CAR primarily remains a function of Tier I capital (98%), showing significant room to support expansion (through Tier II capital).

PROFILE

- HMB, commencing operations in 1992, is listed on all three bourses of Pakistan. The bank is a 51% owned subsidiary of HBZ, incorporated in Switzerland. HMB is a leading player in trade financing and has a sizeable market share in the foreign trade. The bank has a nationwide network of 120 branches (including 4 Islamic banking branches) spread over 19 cities with high concentration in Karachi and Lahore.
- The CEO, Mr. Anjum Iqbal, is a senior banker and has over three decades of local and international banking experience while serving at various locations and senior management positions. A highly professional team of senior executives including the executive director, who plays a pivotal role in evolving the bank's strategy as well as its implementation, assists the Chief Executive.