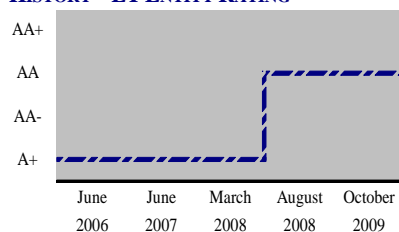


**The Pakistan Credit Rating Agency Limited**
**RATINGS (OCTOBER 2009)**
**ROYAL BANK OF SCOTLAND LIMITED**

	NEW*	PREVIOUS
<b>ENTITY</b>		
Long Term	AA	AA
Short Term	A1+	A1+

**TFCs (UNSECURED, SUBORDINATED, AND LISTED)**
**PKR 800mln** AA- AA-

\*The ratings have been placed on 'RATING WATCH NEGATIVE'
**HISTORY – LT ENTITY RATING**

**FINANCIAL DATA**

	PKR (mln)		
	30-Sep-09	31-Dec-08	31-Dec-07
Total Assets	96,107	108,092	107,536
Equity	6,841	8,276	5,089
Net Income	(1,433)	(517.7)	(1,565)
Equity / Total Assets %	7.1	7.7	4.7
CAR%	11.4	11.7	8.4

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**TFC ISSUE**

- RBSL has an outstanding unsecured subordinated TFC, issued in February 2005 for a tenor of 8 years. The instrument carries mark-up at a floating rate of latest 6-month KIBOR plus 1.9%, payable semi-annually. Principal redemption will be in four equal annual installments commencing from Aug-10.

**RATING RATIONALE AND KEY DRIVERS**

- The ratings reflect RBSL's association with the Royal Bank of Scotland Group Plc (RBSG) which is majority owned by the Government of UK. In Feb 2009, RBSG announced its intention to explore new ownership for its businesses including Pakistan as part of its strategy. As a result, the Group has lately signed a share sale agreement with MCB Bank Limited. However, there have been delays in execution of this transaction. Meanwhile, the bank's overall profile is under pressure on account of, i) absence of any future business strategy, ii) increased impairment in the loan book, and iii) weakening franchise of the bank.
- Given the uncertainty regarding the timely execution of sale transaction or the parent's strategy if the transition does not happen, the ratings are placed on rating watch negative. Nevertheless, the ratings incorporate RBSG's assurance to continue supporting its Pakistan's operations.

**ASSESSMENT**

- Towards the end of 2007, a consortium led by RBSG acquired worldwide operations of ABN AMRO Bank N.V. As a result, ABN AMRO's Pakistan subsidiary was acquired by RBSG which subsequently was renamed to Royal Bank of Scotland Limited (RBSL) in July 2008. However, lately RBSG's own financial profile started deteriorating on account of global financial crises generally and the bank's significant exposure in structured mortgage products in particular. Subsequently towards the end of 2008, it was nationalized by the government of UK. This resulted into a change in focus of the group as instituted by the new shareholder and the group decided to sell its operations in Pakistan among few other operations worldwide. In this context, RBSG entered into an agreement sale transaction with MCB Bank Limited to sell its shareholding in Aug09. Given the delay in execution of this transaction, the performance of the bank is expected to remain under stress, going forward.
- RBSL, a medium size bank in Pakistan in terms of assets, endeavored to keep up with the pace of the industry with a key focus on SME and consumer segment for future growth. However, the general slow down in local economy coupled with increasing interest rates created a challenging operating environment, which undermined the bank's ability to achieve its overall growth targets in recent periods (total assets growth; 9MCY09:-7.5%; CY08:0.5%).
- The loan book of the bank comprises working capital loans (35%), followed by fixed investment(20%), and trade finance loans (16%) to corporates (56% of total loan book) and SMEs (16% of the total loan book) at end Sep-09 while consumer segment constitutes around 23% of the loan portfolio. RBSL's sector wise exposure is dominated by textile, fertilizer, power and telecom sectors with the concentration of top twenty exposures at 23% at end-Sep09. During 9M09, there was a significant dip in advances portfolio (growth at end 9M09: -13%; 2008:7%) on account of weakening demand from private sector and the bank's conservative stance on fresh disbursements. Currently the bank, with an aim to rationalize its operations, is deploying its funds mainly in low risk and liquid government securities, particularly T-bills, while shredding off its high cost fixed deposits to manage its cost structure.
- RBSL has witnessed significant deterioration in its asset quality (Non Performing Loans as percentage of Gross Finances: 18% at end-Sep09; 10% at-end-Dec08). Major part of impaired loan book is constituted by exposures mainly to clients in textile, power, engineering and communication sectors. Overall performance of the bank remained weak owing to, shrinking spreads, and relatively higher level of provisioning. Going forward, given the likely selloff to a new sponsor, the management intends to maintain the status quo in terms of the bank's operations.
- The bank is in compliant with all regulatory requirements related to capital. However, without a clear strategy and increasing impairment in the loan book, the risk absorption capacity is expected to further weaken (net NPLs to equity; 9M09:38%; 2008: 25%; 2007:10%). Moreover, material delay in reviving the bank's operations in line with challenging dynamics of the industry may further impact the franchise of the bank.

**PROFILE**

- RBSL, listed on all the stock exchanges in the country, is operating with 79 branches in more than 24 cities. RBSG, the parent of RBSL is 70% owned by Government of UK, has a consolidated asset base of more than US\$3,300bln at end Jun-09. RBSG has a long-term rating of 'AA-' from Fitch. In Feb09, RBSG announced to sell its operations in fifteen countries (business operations in more than 50 countries). Consequently, in Aug09 RBSG has entered into a share purchase agreement with MCB to sell its 99.37% stake in RBSL for US\$87mln.
- RBSL's BoD comprises seven members out of which four hold senior management positions in international operations of RBSG and three are independent directors. The Chairman, Mr. Muhammad Aurangzeb, is currently serving as Head of Global South East Asia and Pakistan. The bank's president, Mr. Shahzad Naqvi, has extensive experience with renowned local and multinational financial sector entities. He is assisted by a team of qualified and experience professionals.