

**RATINGS (JUNE 2010)**
**ROYAL BANK OF SCOTLAND LIMITED (RBSL)**

	New	Previous
<b>Entity</b>		
Long Term	AA	AA
Short Term	A1+	A1+
<b>TFC Issue(PKR800mln) unsecured, subordinated,</b>	AA-	AA-
<b>Outlook</b>	-	Negative

\*The Ratings are on “Rating Watch”.

LT ENTITY RATING - HISTORY						
AA+						AA+
AA				RW	RW	AA
AA-						AA-
A+						A+
A-						A-
	Jun-07	Mar-08	Aug-08	Oct-09	Jun-10	
	Negative Outlook			RW Rating Watch		

**FINANCIAL DATA (PKR IN MLN)**

	31-Mar-10 <sup>^</sup>	31-Dec-09	31-Dec-08
Total Assets	87,987	93,438	108,092
Equity	5,793	6,937	8,276
Net Loss	(1,144)	(1,338)	(518)
Equity / Total Assets %	6.6	7.4	7.7
CAR%	10.4	11.4	11.7

<sup>^</sup> Based on un-audited results for 3 months ended Mar 31, 2010

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**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 purchase agreement with Faysal Bank Limited. The transaction is expected to be executed by end third quarter CY10.
- The successful and timely execution of sale transaction remains critical as the bank’s standalone profile has weakened owing to increased impairment in the loan book, and continuing business losses. Nevertheless, the ratings incorporate RBSG’s assurance to continue supporting Pakistan’s operations. Pending the completion of acquisition of the bank by the new sponsor, the ratings would remain on “Rating Watch”.

**ASSESSMENT**

- In past few years, RBSL remained target of key banking acquisitions. The current sponsor of the bank - Royal Bank of Scotland Group Plc – was nationalized by the Government of UK in November 2008 as a consequence of the global financial crises. 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 the later half of CY09, the group entered into an agreement with a local bank for sale of RBSL. However, the transaction could not materialize. Lately, the group has signed a share purchase agreement with Faysal Bank Limited. The transaction is expected to be completed by end 3QCY10.
- Subsequent to announcement of the sponsor to sale bank’s operation, RBSL focused mainly on consolidating its existing operations. The loan book shrunk by more than 25 beginning 2009, whereby maturing loans are being deployed in low risk government securities, suppressing the spreads to certain extent as well. Additionally, increasing infection rate in existing loan book also contributed in a decline in earning assets on YoY basis in 2009. Thus, overall performance of the bank remained weak owing to shrinking spreads, and relatively higher level of provisioning. During 1Q10, the bank’s performance further deteriorated owing to lower business volume and higher provisioning.
- RBSL’s sector wise exposure is dominated by textile, transport, chemicals, and food sector. During CY09 the bank has witnessed significant deterioration in its asset quality (Non Performing Loans as percentage of Gross Finances: 21% at end Mar10; 10% at end Dec08). Major part of impaired loan book constitutes textile, power, and consumer segments. Nevertheless, the coverage of infected portfolio remains adequate (74% at end Mar-10).
- The overall deposit base of the bank also declined (CY09: -19.6%; CY08: -12.4%) as the bank continued to shed high cost deposits to control the funding costs. However, the bank maintained relatively high liquidity (Liquid Assets to Deposits and Borrowing: 1Q10: 48%; CY08: 34%).
- The bank is compliant with minimum Capital adequacy ratio (10.4% at end Mar-10; 11.4% at end Dec-09). However, due to significant loss in 1Q10, bank’s equity is below the minimum capital requirement. The risk absorption capacity is expected to further weaken as reflected in residue drag of unprovided NPLs to equity of 48% at end Mar10 (CY09:46%; CY08: 25%).
- Going forward, timely and smooth execution of the sale transaction is considered critical for the bank. Given ongoing losses and, in turn, weakening risk absorption capacity, material delays would significantly erode the bank’s ability to manage challenging dynamics of the industry. Nevertheless, the integration and overcoming constraints of current operations of RBSL would be challenging for the acquiring 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 and 68% owned by Government of UK, has a consolidated asset base of more than US\$2,396bln at end Mar-10. RBSG is rated by all three major international rating agencies (Long term Rating: Moody’s: A1; Standard & Poor’s: A; Fitch: AA-). In Feb09, RBSG announced to sell its operations in fifteen countries (out of business operations in more than 50 countries). Lately, RBSG has entered into a share sale agreement with Faysal Bank to sell its 99.37% stake in RBSL for US\$ 50.5mln (PKR 4,298mln).
- 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. Few changes at top management level have taken place in the bank. While various senior employees have left, recently the bank’s president, Mr. Shahzad Naqvi, also resigned. Mr. Salman Sarwar Butt, Head of Retail Banking, is acting president.

**PROFILE**

- 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.