



STANDARD CHARTERED BANK (PAKISTAN) LIMITED (SCBP)

Ratings (June 2008)

Standard Chartered Bank (Pakistan) Limited (SCBP)

	New	Previous
Entity		
Long-Term	AAA	AAA
Short-Term	A1+	A1+
TFCs Issue		
1 st Issue [^] PKR 750mln	-	AAA
2 nd Issue PKR 750mln	AAA	AAA
3 rd Issue PKR 1000mln	AAA	AAA

[^] The 1st TFC Issue has been redeemed fully, hence, its rating is withdrawn

Financial Data

PKR (mln)

	31-Dec -07	31-Dec -06
Total Assets	255,545.2	246,317.8
Equity	43,340.6	40,558.8
Net Income	2,766.8	5,709.5
Equity/Total Assets %	16.96	16.47

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TFC Issues

SCBP has two listed unsecured subordinated TFCs outstanding, 2nd Issue and 3rd Issue. The bank issued its second unsecured subordinate TFCs (PKR 750mln) for a tenor of 7 years during December 2003. The profit payment is at a floating rate of latest cut-off yield of 5 years PIB plus 75bps with a floor of 5% and cap of 10.75%. The major principal redemption will be in six unequal installments, commencing from the 54th month of issue. The third TFC of PKR 1,000 million was issued in January 2006, for 7-year tenor, with profit payable at a floating interest rate of 6-months KIBOR + 2%. Principal redemption will be in six unequal installments, commencing from the 54th month of issue.

RATING RATIONALE AND KEY DRIVERS

The ratings reflect the bank's sound financial profile, established brand equity, quality management team and positive growth trends. Underpinned by these strengths, the bank forges ahead with its strategy to boost revenues capitalizing upon its integrated operating platform and expanded distribution footprint. The ratings also recognize the sound financial strength and international profile and experience of the parent – Standard Chartered Bank (SCB) – in the emerging markets banking industry as a key rating factor. SCBP, being an important player in the SCB group, continues to benefit from the technical resources and cumulative expertise developed at the group level, resulting in robust risk management systems and processes, and product innovation.

Ratings are dependent upon the management's ability to strengthen its business plan to maintain the bank's relative positioning in the sector with a prudent control over the associated risks. Any further material deterioration in the quality of assets remains a critical concern for the ratings.

ASSESSMENT

CY07 has been SCBP's first year of operations as a merged entity. The balance sheet showed only a meager increase in size as the bank focused upon re-aligning its strategy to capitalize upon the recent acquisition. The bank maintains the highest spreads in the sector owing to relatively higher asset yields and lower funding costs. Contribution of fee income to revenue remains healthy. Operating costs are higher as the bank expands the branch network and completes the integration during the year. Pre-provisioning operating profit shows significant growth, however, pre-tax profitability took the hit owing to higher provisioning due to changes in provisioning criteria and increase in non-performing loans (NPLs). During 1QFY08, profitability remains depressed with rising impairment losses and high operating expenses. Asset quality deteriorates further as NPLs maintain an increasing trend.

The bank has ambitious growth plans. It plans to continue expanding the branch network to deliver upon its vision of being a "locally embedded international bank". In order to achieve these plans, it has embarked upon a unique "journey of transformation" through: (i) growth in its distribution footprint, (ii) innovative products and services, (iii) talented and diverse teams, and (iv) sustainable business strategy based upon community investment. SCBP expanded its distribution footprint by 26 branches in 2007, adding another 35 branches during the first half of the current year. The bank now operates with 176 branches in 41 cities. Pakistan's consumer banking operations ranks sixth in the Group, while in terms of branch network, it is at third position. In line with the group's overall increasing focus on consumer, SME and Islamic Banking business, SCBP has further expanded the product suite in both these areas. With its focus on high yielding segments and relatively lower cost of deposits amongst peers, it is enjoying one of the highest spreads within the sector. Going forward, spreads could take a moderate hit with SBP's recent directive for higher minimum required return for saving deposits. However, the bank's targeted move to re-profile its deposit mix in favor of low-cost deposits, reducing the proportion of high-cost term deposits would offset the impact of this development to some extent.

The NPLs as a proportion of total advances increased substantially in 2007, mainly in unsecured consumer loans. Total loans written off against provisions during the year were PKR3.7bln. The increase in NPLs was due to softening of macro economy and, amongst other factors, the impact arising from the integration on the collection infrastructure. However, the loss coverage ratio is strong, given the group's standards applied for provisioning are more stringent than local regulations. However, the management has taken appropriate measures to faster recoveries, while also realigning its policies in line with the changing market dynamics. With the recent monetary tightening, delinquencies are expected to mount as rising borrowing costs have restricted the repayment capacity of highly leveraged individual borrowers, hence leading to defaults.

SCB, as a policy, monitors and manages risk on a group wide basis. In addition, a proactive and customized risk management framework is adopted employing stronger systems and controls. Risk based pricing is in place for the entire wholesale banking portfolio, while, the consumer banking portfolio is extensively checked, at regular intervals, for existing and potential delinquency. To avoid conflict of interest, the risk function is completely separate from the business functions. The bank has decided to adopt the COSO Framework of internal controls in 2008.

The bank has one of the highest capitalization levels in the sector. However, it is not reflected in CAR (end-Mar08: 11.49%), as the bulk of the equity represents goodwill, which is deducted for the purpose of computation of regulatory capital requirement. Given the strong performance prospects of the bank, the expected increase in equity through profit retention is likely to comfortably support the targeted growth.

PROFILE

Standard Chartered Bank (Pakistan) Limited (SCBP), a majority owned subsidiary (around 99%) of Standard Chartered Bank, UK, was incorporated in Pakistan in Jul06. SCBP acquired a controlling stake (95%) in Union Bank Limited (UB). The bank commenced its business following the merger of Union Bank Limited and Standard Chartered Bank, Pakistan Branches, with and into SCBP, effective December 30, 2006. The seven member BoD of the bank is diverse in terms of experience and background and provides strong guidance to the management. The bank's CEO has an extensive local and international banking experience. He has been with the group since 1991, and has held various senior positions, including the CEO of Pakistan's operations since July 2003.

The ultimate holding company for the Standard Chartered Group is Standard Chartered plc, a company incorporated in UK. Standard Chartered has a history of over 150 years in banking and operates in world's emerging markets with an extensive global network of over 1,400 branches (including subsidiaries, associates, and joint ventures), in over 50 countries in the Asia Pacific region, South Asia, the Middle East, Africa, the United Kingdom, and the Americas. Standard Chartered Bank, UK carries an international rating of 'A+' by Standard & Poor's and Fitch.