

SONERI BANK LIMITED (SBL)

RATINGS (JUNE 2006)

SONERI BANK LIMITED

RATINGS

	New	Previous
Entity		
Long Term	AA-	AA-
Short Term	A1+	A1+
TFCs		
<i>Unsecured, listed</i>		
1 st Issue	A+	A+
(PKR 1,200mln)		

HISTORY – LT ENTITY RATING

AA						
AA-						
A+						
	May 2001	Jun 2002	Jun 2003	Jun 2004	Mar 2005	Jun 2006

FINANCIAL DATA

(Amounts in PKR mln)

	31-Dec-05	31-Dec-04
Total Assets	63,345.1	49,851.9
Equity	3,636.6	2,878.8
Net Income	920.2	648.4
ROA (%)	1.63	1.49
ROE (%)	28.25	25.38
Equity / Total Assets (%)	5.74	5.77
SBP CAR (%)	11.68	8.31

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TFC ISSUE

SBL issued unsecured subordinated TFCs of PKR 1,200mln for a tenor of 8 years in May 2005. The profit payment, to be made semi-annually, will be based on 6 month KIBOR *plus* 160bps. The principal will be redeemed in four equal semi-annual installments starting from the 78th month (October 2011) from the issue date. The TFC holders are exposed to a relatively higher risk, as the obligations towards the TFC holders are subordinate to those of other creditors including depositors of the bank.

RATING RATIONALE ASSESSMENT

- The ratings reflect the bank's business philosophy that encompasses a conservative stance towards risk while maintaining a stable, albeit modest, asset growth. The bank, despite consistently higher growth by some peers, intends to continue its prudent asset deployment strategy, while gradually expanding its outreach. Meanwhile, it is working on enhancing its fee-based earnings mainly through investment banking activities. The ratings also take into account the management's structured efforts to further strengthen the risk management systems.
- The bank, during 2005 and onwards, maintained its focus on working capital financing, constituting around 84% of total finances at end-05. Importantly, around half of these exposures are in the form of trade financing that inherently has a low-risk profile. Meanwhile, there is a visible shift in the composition of the bank's advances portfolio in favor of SMEs (05: 38%, 04: 27%) from corporates (05: 58%, 04: 70%). This, to a great extent, is an outcome of intensified competition amongst banks for good quality corporate credits exerting pressure on pricing. The bank, by concentrating on SMEs, has been able to build a relatively high return advances book, while achieving volume expansion. The trade volume handled by the bank (05: US\$ 1.6bln, 04: US\$ 1.3bln) increased in line with the overall growth in the economy with the bank maintaining its relative share of around 4%. However, within non-fund based revenues, the bank could not increase its income from dealing in foreign currencies, despite higher volumes, due to intensifying competition amongst banks. Nevertheless, higher spreads, reduction in cost-to-revenue ratio and lower effective tax rate helped the bank in achieving YoY improved performance – measured in terms of both ROA & ROE. During 1Q06, the bank's spreads were under pressure due to certain high-cost deposits mobilized towards the end of previous year. However, the impact of lower spreads on the bottom line was masked by substantial capital gains on equities realized during this period.
- The management is cognizant of increasing pressure on spreads and plans to manage the impact on profitability by volume expansion, going forward. To achieve the said growth, the bank intends to capitalize on its established experience in niche market of working capital financing. However, there would be increased focus on SMEs and sectors other than textiles. Meanwhile, the bank is continuing with geographical network expansion, which, in addition to providing access to newer markets for credit growth, is expected to help in low cost deposit mobilization. Although the bank has developed a range of consumer products, it would follow a conscious expansion strategy in this segment.
- The bank is implementing a comprehensive risk management program, which includes a) up-gradation of the core banking software, b) establishing an independent credit risk management department, and c) strengthening of internal control function. The ongoing program is targeted for full implementation by the end of current year. The bank has already established middle office to manage market risk emanating from treasury and forex operations. The bank is ahead of some of its peers for timely implementation of requirements under Basel II. The consultancy firm, engaged for performing gap analysis, is expected to submit its report shortly recommending the desired actions and preferred timeline for the same.
- Soneri Bank enjoys sound asset quality with NPLs being maintained at around 1% of the finances at end-2005. These NPLs are fully provided. Going forward, given the management's focus on working capital financing with a careful diversification in other areas, the bank is expected to maintain its asset quality.
- SBL's capital structure, measured in terms of equity-to-assets, was maintained at a comfortable level on YOY basis on the back of limited cash distribution. However, its CAR due to sustained growth in risk-weighted assets over the years was close to the statutory permissible limit. The bank, therefore, issued subordinated debt during 2005, which, with its extended tenor, is supporting the CAR to undertake growth. Additionally, the bank has carried out revaluation of its fixed assets generating further Tier 2 capital. The management is confident of meeting the increasing paid-up capital requirement through internal generation. However, the sponsors have both willingness and resources to meet the shortfall, if any.

BACKGROUND

- SBL, commencing its operations in 1992, currently operates a network of 60 branches. The Feerasta family, owners of the Rupali group, holds the controlling stake in the bank. The group's primary activities are centered on the synthetic textile industry. The group, through Ferrasta family members and nominees, maintains a dominant position on the bank's board of directors. The President and Chief Executive, a banker with over four decades of domestic and international banking exposure, manages the operations of the bank through a team of experienced professionals.