The Pakistan Credit Rating Agency Limited

MCB BANK LIMITED
(MCB)
ENTITY RATINGS REPORT

	NEW [DEC-17]	PREVIOUS [JUN-17]
Entity		
Long Term	AAA	AAA
Short Term	A1+	A1+
Unsecured, Subordinated, listed TFCs of PKR 4,198mln	AAA	AAA
Outlook	Stable	Stable

REPORT CONTENTS

DECEMBER 2017

Profile & Ownership

- MCB Bank Limited (MCB), incorporated in 1947, is listed and is the fourth largest bank in terms of its share in total customer deposits (8%) as at end-Sep17
- One of the largest branch network with a distinct franchise (1,405 domestic online branches at end-Sep17)
- MCB Bank is majority owned by Nishat group (~36%), a prominent business conglomerate, followed by Malayan Banking Berhad (Maybank) of Malaysia, has ~19% stake in MCB since May-08
- NIB Bank Limited has been amalgamated with and into MCB Bank Limited with effect from 7th July 2017

Governance

- Mian Mohammad Mansha – one of the leading businessman and the man behind Nishat Group – is the chairman of MCB's thirteen-member board of directors
- President & CEO Mr. Imran Maqbool is an executive director while others are non-executive directors including two representatives of Maybank
- To improve its governance structure, the board ensures effective monitoring of the bank's overall operations through its eight committees

Management

- Mr. Imran Maqbool joined MCB in 2002 and has been the CEO since December 22, 2012. He possesses over three decades of commercial banking experience
- Assembled an experienced team of senior management to assist the CEO
- The bank, with a largely horizontal organizational structure, includes business and support groups along with divisions reporting to CEO

Risk Management

- Assets Rehabilitation Group (ARG) currently handles non-performing loan portfolio with a recovery yield of ~20%
- Top twenty funded exposure rose by 2% on YoY basis to 32% (CY15: 30%), although in line with peers, remains high. However, asset quality is good
- Proportion of short term loans including working capital and trade finance loans in the total advances declined to 44% (CY15: 48%)
- The infection ratio of the bank has been continuously improving on a standalone basis, however, with amalgamated numbers of NIB the infection ratio has been distorted (9MCY17: 10%, CY16: 5.9%. 9MCY16: 6.2%, CY15: 6.1%)
- Investment portfolio jumped by 37% YoY to PKR 676bln during 9MCY17 (9MCY16: PKR 493bln). The bank's investment portfolio constitutes 52% of the asset base and government securities continue to dominate the overall investment book
- The banks PIBs have matured early as compared to its peers, hence, giving it first advantage over competitors to park its excess liquidity in other avenues

Business Risk

- Decent growth was witnessed in gross finances
- Interest revenue witnessed a rise of 7%, attributable to high volumetric growth
- Improvement in cost of funds was not sufficient enough to sustain NIMR at last year's level, hence recorded a decline of 7%
- With high operational expenses attributable to the merger; resulted in increase in the cost to total net revenue on a YoY basis (9MCY17: 47%, 9MCY16: 38%)
- MCB will continue with its current strategy of lending to premier corporates with sustained focus on government exposure. At the same time, beefing up of the consumer and SME book is also anticipated amidst improving macro fundamentals

Financial Risk

- Stable and rising deposit base, exhibited a growth of 28% during 9MCY17, owing to the merger; outpacing the industry's growth
- Established brand and extensive branch network, helped in reporting a high CASA of 94%, highest in the industry
- Historically MCB enjoyed one of the highest CAR in the industry, however, post-merger, the CAR has declined to 17%. It is pre-dominantly constituted of Tier-I capital (15.2%) – a factor of healthy profitability and reserves

RATING RATIONALE

The ratings take note of MCB's sustained financial profile, reflected in very strong capitalization, sound liquidity and diverse deposit base. This has been enabled by the bank's able parentage, wherein a diverse mix of sponsors - mainly led by Nishat Group - has been providing an effective oversight. The ratings factor in MCB's strong market positioning, supported by its well established brand name and substantial out reach. MCB has the highest CASA in the industry, with lowest cost of funds amongst all players. The bank lately has added sizeable chunk to its deposit base, slightly inching it up. The bank continues with its current strategy of lending to premier corporates with sustained focus on government exposure. At the same time, beefing up of the consumer and SME book is also anticipated amidst improving macro fundamentals. The prevailing interest rate environment is a challenge especially with the drying stream of PIBs. The bank has established an Islamic Banking subsidiary, thereby, becoming the first conventional bank to do so. NIB Bank Limited was merged with and into MCB in July-17. Post-merger, MCB's risk profile has sustained - which bodes well for the bank.

KEY RATING DRIVERS

The ratings are dependent on the bank's ability to hold its existing position in the banking sector. Any deterioration in the perceived strength of the bank or ownership with consequent impact upon its governance efficacy would have negative implication. Further strengthening of human resource would be vital.

INDUSTRY SNAPSHOT

The banking sector experienced substantial expansion in its deposit base (2016: 14%). Building on the uptick in the economy, advances also grew by a sizeable margin after a lag of many years. Given GDP growth in FY17 and other macro-economic fundamentals, credit expansion is foreseen. Hence, CAR is going to be a challenge, as profits would also suffer due to PIBs maturities.

MCB Bank Limited

PKR mln

BALANCE SHEET	30-Sep-17	31-Dec-16	31-Dec-15	31-Dec-14
	9M	Annual	Annual	Annual
Earning Assets				
Advances (Net of NPLs)	437,687	345,990	312,258	300,410
Debt Instruments	7,150	5,899	9,927	8,246
Total Finances	444,837	351,888	322,185	308,656
Investments	675,118	550,030	558,876	502,891
Others	18,317	10,063	12,651	8,083
	1,138,272	**911,981**	**893,711**	**819,630**
Non Earning Assets				
Non-Earning Cash	93,317	71,313	57,372	43,105
Net Non-Performing Finances	3,217	1,990	1,867	3,149
Fixed Assets & Others	73,125	66,529	63,679	68,747
	171,186	**139,833**	**122,918**	**115,001**
TOTAL ASSETS	**1,309,458**	**1,051,814**	**1,016,630**	**934,632**
Interest Bearning Liabilities				
Deposits	962,500	781,430	708,091	688,330
Borrowings	140,406	74,515	118,459	59,543
	1,102,906	855,945	826,551	747,872
Non Interest Bearing Liabilities	50,063	54,242	52,279	56,655
TOTAL LIABILITIES	**1,152,969**	**910,187**	**878,829**	**804,527**
EQUITY (including revaluation surplus)	**156,489**	**141,627**	**137,800**	**130,104**
Total Liabilities & Equity	**1,309,458**	**1,051,814**	**1,016,630**	**934,632**

INCOME STATEMENT	30-Sep-17	31-Dec-16	31-Dec-15	31-Dec-14
	9M	Annual	Annual	Annual
Interest / Mark up Earned	55,620	67,422	80,532	77,269
Interest / Mark up Expensed	(24,164)	(23,655)	(31,210)	(33,757)
Net Interest / Markup revenue	**31,456**	**43,767**	**49,322**	**43,512**
Other Operating Income	13,584	15,901	16,705	12,747
Total Revenue	**45,040**	**59,668**	**66,027**	**56,259**
Other Income / (Loss)	272	320	410	197
Non-Interest / Non-Mark up Expensed	(21,210)	(23,260)	(23,560)	(21,668)
Pre-provision operating profit	24,102	36,728	42,877	34,788
Provisions	1,897	(654)	(544)	1,941
Pre-tax profit	25,999	36,075	42,333	36,729
Taxes	(6,860)	(14,184)	(16,782)	(12,405)
Net Income	**19,138**	**21,891**	**25,550**	**24,325**

Ratio Analysis	30-Sep-17	31-Dec-16	31-Dec-15	31-Dec-14
	9M	Annual	Annual	Annual
Performance				
ROE	20%	19%	23%	24%
Cost-to-Total Net Revenue	47%	39%	36%	39%
Provision Expense / Pre Provision Profit	8%	2%	1%	6%
Capital Adequacy				
Equity/Total Assets	11%	11%	11%	11%
Funding & Liquidity				
Liquid Assets / Deposits and Borrowings	68%	73%	75%	75%
Advances / Deposits	46%	45%	44%	44%
CASA deposits / Total Customer Deposits	93%	94%	93%	91%
Intermediation Efficiency				
Asset Yield	7%	8%	10%	10%
Cost of Funds	3%	3%	4%	5%
Spread	4%	5%	6%	6%
Outreach				
Branches	1,416	1,238	1,246	1,232

**9M numbers are pro-rated and annualized where applicable*

CREDIT RATING SCALE & DEFINITIONS

Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

LONG TERM RATINGS

AAA	**Highest credit quality.** Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments.
AA+ AA AA-	**Very high credit quality.** Very low expectation of credit risk. Indicate very strong capacity for timely payment of financial commitments. This capacity is not significantly vulnerable to foreseeable events.
A+ A A-	**High credit quality.** Low expectation of credit risk. The capacity for timely payment of financial commitments is considered strong. This capacity may, nevertheless, be vulnerable to changes in circumstances or in economic conditions.
BBB+ BBB BBB-	**Good credit quality.** Currently a low expectation of credit risk. The capacity for timely payment of financial commitments is considered adequate, but adverse changes in circumstances and in economic conditions are more likely to impair this capacity.
BB+ BB BB-	**Moderate risk.** Possibility of credit risk developing. There is a possibility of credit risk developing, particularly as a result of adverse economic or business changes over time; however, business or financial alternatives may be available to allow financial commitments to be met.
B+ B B-	**High credit risk.** A limited margin of safety remains against credit risk. Financial commitments are currently being met; however, capacity for continued payment is contingent upon a sustained, favorable business and economic environment.
CCC CC C	**Very high credit risk**. Substantial credit risk "CCC" Default is a real possibility. Capacity for meeting financial commitments is solely reliant upon sustained, favorable business or economic developments. "CC" Rating indicates that default of some kind appears probable. "C" Ratings signal imminent default.
D	Obligations are currently in default.

SHORT TERM RATINGS

A1+: The highest capacity for timely repayment.

A1:. A strong capacity for timely repayment.

A2: A satisfactory capacity for timely repayment. This may be susceptible to adverse changes in business, economic, or financial conditions.

A3: An adequate capacity for timely repayment. Such capacity is susceptible to adverse changes in business, economic, or financial conditions.

B: The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions.

C: An inadequate capacity to ensure timely repayment.

Outlook (Stable, Positive, Negative, Developing)
Indicates the potential and direction of a rating over the intermediate term in response to trends in economic and/or fundamental business/financial conditions. It is not necessarily a precursor to a rating change. 'Stable' outlook means a rating is not likely to change. 'Positive' means it may be raised. 'Negative' means it may be lowered. Where the trends have conflicting elements, the outlook may be described as 'Developing'.

Rating Watch
Alerts to the possibility of a rating change subsequent to, or in anticipation of, a) some material identifiable event and/or b) deviation from expected trend. But it does not mean that a rating change is inevitable. A watch should be resolved within foreseeable future, but may continue if underlying circumstances are not settled. Rating Watch may accompany Outlook of the respective opinion.

Suspension
It is not possible to update an opinion due to lack of requisite information. Opinion should be resumed in foreseeable future. However, if this does not happen within six (6) months, the rating should be considered withdrawn.

Withdrawn
A rating is withdrawn on a) termination of rating mandate, b) cessation of underlying entity, c) the debt instrument is redeemed, d) the rating remains suspended for six months, e) the entity/issuer defaults., or/and f) PACRA finds it impractical to surveill the opinion due to lack of requisite information

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Regulatory and Supplementary Disclosure

Rated Entity

Name of Rated Entity MCB Bank Limited
Sector Banking
Type of Relationship Solicited

Purpose of the Rating Independent Risk Assessment
Regulatory Requirement

Rating History

Dissemination Date	Long Term	Short Term	Outlook	Action
29-Dec-17	AAA	A1+	Stable	Maintain
19-Jun-17	AAA	A1+	Stable	Maintain
24-Jun-16	AAA	A1+	Stable	Maintain
24-Jun-15	AAA	A1+	Stable	Maintain
26-Jun-14	AAA	A1+	Stable	Maintain

Related Criteria and Research

Rating Methodology Bank Rating Methodology
Sector Research Banking Sector - Viewpoint | Jun-17

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Rating Team Statement

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Regulatory and Supplementary Disclosure

Rated Entity

Name of Issuer	MCB Bank Limited
Name of Issue	MCB | TFC II
Sector	Banking
Type of Relationship	Solicited
Purpose of the Rating	Regulatory Requirement Independent Risk Assessment

Rating History

Dissemination Date	TFC	Rating Action
29-Dec-17	AAA	Maintain
6-Oct-17	AAA	Upgrade
15-Jun-17	A+	Maintain
13-Dec-16	A+	Rating Watch
24-Jun-16	A+	Maintain
26-Jun-15	A+	Maintain
26-Jun-14	A+	Maintain

Instrument Details

Nature of Instrument	Size of Issue	Tenor	Trustee	Security
TFC (Sub-ordianted, Listed)	PKR 4,198mln	8 years	Pak Brunei Investment Company	Unsecured

Amortization Schedule

See Annexure A

Related Criteria and Research

Specific Methodology:	Bank Rating Methodology
Research:	Banking Sector - Viewpoint | Jun-17

Rating Analysts

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Loan Amount (PKR) 4,198,000,000
Tenor (Years) 8 years
Rate 6MK + 1.15% (Assumed Kibor: 6.12%)

PKR mln

Installment	MCB Bank Limited	Principal	Mark Up	Total Installment	Outstanding
	MCB | TFC II				4,198
1	Dec-14	0.8	#VALUE!	#VALUE!	4,197
2	Jun-15	0.8	168	168	4,196
3	Dec-15	0.8	167	168	4,195
4	Jun-16	0.8	157	158	4,195
5	Dec-16	0.8	154	155	4,194
6	Jun-17	0.8	151	152	4,193
7	Dec-17	0.8	154	155	4,192
	Dec-17				
	Oct-17				
8	Jun-18	0.8	151	152	4,191
9	Dec-18	0.8	154	154	4,190
10	Jun-19	0.8	151	152	4,190
11	Dec-19	0.8	154	154	4,189
12	Jun-20	0.8	152	153	4,188
13	Dec-20	0.8	153	154	4,187
14	Jun-21	0.8	151	152	4,186
15	Dec-21	0.8	153	154	4,185
16	Jun-22	4,185	151	4,336	0

Call option exercisable