The Pakistan Credit Rating Agency Limited

HABIB METROPOLITAN BANK LIMITED

	NEW [DEC-17]	PREVIOUS [JUNE-17]
Entity		
Long Term	AA+	AA+
Short Term	A1+	A1+
Outlook	Stable	Stable

REPORT CONTENTS

DECEMBER 2017

Assets:
- The bank's liquidity, in terms of its Liquid Assets-to-Deposits and Borrowings ratio, decreased on YoY basis, to 72% at end-Sep17 (end-Sep16: 77%), comprising pre-dominantly government entities.
- The advances to deposit ratio (ADR) remained increased slightly (Sep17: 35%, Sep16: 33%).
- Gross advances increased by an impressive 17% (Sep17: PKR 170.1bln: Sep16: PKR 145.1bln).
- The contribution of the bank's CASA remained steady (Sep17:55%%, Sep16: 56%). The bank's share in this segment remains low in comparison to its peer banks.

Funding
- The main source of HMB's funding is its deposit base, constituting around 80% of the total liabilities at end-Sep 17.

Credit Risk
- The NPL's of the bank increased (Sep17: PKR 18.474mln, Sep16: PKR 15.623mln), however the infection ratio simultaneously improved to 10% (Sep16: 12.96%) on the back of increased advances.

Market Risk
- HMB's investment portfolio witnessed a minor increase of ~2% (Sep17: PKR 375bln, Sep16 PKR 370bln) and constitutes 65% of the total earning assets at end-Sep17.
- HMB is gradually shifting its exposure from PIB's to T-bills on the account of reduced interest rate from PIBs.

Performance
- The bank's net interest revenue increased by ~18% owing to reduced interest expense.
- Increase in non-interest expenses (Sep17: PKR 8.117mln, Sep16: PKR 6.990mln) led to reduction in bank's profitability with the net income decreasing to PKR 3.255mln (Sep-16: 3.819mln).
- The asset yield declined by 0.29% (end-Sep17: 5.95%, end-Sep16: 6.24%) Similarly, cost of funds witnessed a decrease (end-Sep17: 3.49%, end-Sep16: 4.16%), thereby reducing the spread by 38bps (end-Sep17: 2.46%, end-Sep16: 2.08%).

Capital
- HMB's paid up capital stands at PKR 10,478mln thus safely meeting the MCR of PKR 10,000mln.
- The bank has a strong CAR (end-Sep17: 16.76%, CY16: 18.15%), with key contribution from Tier I capital (15.83%) and Tier II capital (0.93%).
- The bank's growth trend has been a factor for high CAR.

Business Strategy
- Going forward, the bank aims to target organic growth, mobilization of low-cost deposits and improvement of asset quality.
- Both avenues are areas of attention, as the bank has very low concentration of CASA and continues to have stressed asset quality.

Profile
- Habib Metropolitan Bank (Habib Metro), originally Metropolitan Bank Limited, started banking operations in 1992, and is listed on Pakistan Stock Exchange.
- During 2016, the bank opened 31 new branches across 10 new cities. The bank has a nationwide network of 307 branches at end-Dec16.

Governance and management
- HMB's nine member Board of Directors (BoD) comprises CEO, two representatives of HBZ, two independent directors, three non-executive directors and one nominee of NIT.
- The CEO, Mr. Sirajuddin Aziz, carries experience of over three decades pertaining to domestic and international banking industry.
- A professional team of senior executives assists the Chief Executive.

RATING RATIONALE

The ratings incorporate HabibMetro's association with a diversified and financially strong international bank - Habib Bank AG Zurich (HBZ). This association helps in assimilating the parent's best practices into HabibMetro, while fostering control environment with enhanced level of oversight. The ratings recognize the bank's healthy financial profile reflected in its strong CAR, pre-dominantly constituting Tier-I Capital (17.27% at end Dec-16). The bank has experienced downtrend in profitability which will remain a challenge in days to come. With dynamic competition in the market, holding onto a sustained market share (deposits and advances) with profitable growth has become increasingly difficult. The bank's strategy envisages re-orientation of the bank towards supply chain. The bank experienced relatively high infection compared to most peers, though these are considerably covered. NPL's are high; management's efforts must translate in sustained asset quality - indeed improvement. The bank needs to diversify its deposit base.

KEY RATING DRIVERS

The ratings are dependent on the management's ability to augment its position generally in the banking industry and particularly in its market niche - trade finance. Any weakening in asset quality in turn will put pressure on the bank's profitability and risk absorption capacity.

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.

Habib Metropolitan Bank Limited

BALANCE SHEET	30-Sep-17 9M	31-Dec-16 Annual	30-Sep-16 9M	31-Dec-15 Annual
Earning Assets				
Advances (Net of NPL)	166,375	140,020	138,271	131,589
Debt Instruments	3,768	5,791	6,835	7,156
Total Finances	170,143	145,811	145,107	138,745
Investments	371,377	308,958	363,118	274,080
Others	31,534	16,795	26,588	24,925
	573,054	**471,565**	**534,813**	**437,751**
Non Earning Assets				
Non-Earning Cash	37,882	37,777	30,801	33,962
Deferred Tax	3,146	2,459	2,047	1,939
Net Non-Performing Finances	844	2,812	(1,633)	956
Fixed Assets & Others	12,522	11,994	11,562	15,272
	54,395	**55,042**	**42,778**	**52,129**
TOTAL ASSETS	**627,448**	**526,606**	**577,591**	**489,879**
Interest Bearing Liabilities				
Deposits	474,745	430,888	473,315	403,355
Borrowings	97,902	37,205	46,021	31,463
	572,647	468,093	519,336	434,818
Non Interest Bearing Liabilities	20,239	18,843	19,502	18,234
TOTAL LIABILITIES	**592,886**	**486,936**	**538,838**	**453,052**
	80%		88%	
EQUITY (including revaluation surplus)	**34,562**	**39,670**	**38,753**	**36,828**
Total Liabilities & Equity	**627,448**	**526,606**	**577,591**	**489,879**

INCOME STATEMENT	30-Sep-17	31-Dec-16	30-Sep-16	31-Dec-15
Interest / Mark up Earned	24,696	33,172	25,493	36,850
Interest / Mark up Expensed	(14,309)	(21,410)	(16,715)	(22,466)
Net Interest / Markup revenue	**10,387**	**11,762**	**8,778**	**14,384**
Other Income	4,201	8,836	6,040	9,182
Total Revenue	**14,588**	**20,598**	**14,818**	**23,566**
Non-Interest / Non-Mark up Expensed	(8,117)	(9,420)	(6,990)	(8,801)
Pre-provision operating profit	6,471	11,178	7,828	14,765
Provisions	(728)	(845)	(1,046)	(2,226)
Pre-tax profit	5,743	10,334	6,781	12,539
Taxes	(2,488)	(4,214)	(2,963)	(4,883)
Net Income	**3,255**	**6,119**	**3,819**	**7,656**

Ratio Analysis	30-Sep-17	31-Dec-16	30-Sep-16	31-Dec-15
Performance				
ROE	12%	17%	15%	24%
Cost-to-Total Net Revenue	56%	46%	47%	37%
Provision Expense / Pre Provision Profit	11%	8%	13%	15%
Capital Adequacy				
Equity/Total Assets	6%	7%	6%	7%
Capital Adequacy Ratio as per SBP	17%	18%	#DIV/0!	18%
Funding & Liquidity				
Liquid Assets / Deposits and Borrowings	72%	74%	77%	73%
Advances / Deposits	35%	33%	29%	33%
CASA deposits / Total Customer Deposits	54%	57%	58%	57%
Intermediation Efficiency				
Asset Yield	6%	7%	6%	9%
Cost of Funds	3%	5%	4%	6%
Spread	2%	3%	2%	4%
Outreach				
Branches	333	307	276	276

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STANDARD RATING SCALES & 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 or 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.** "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.

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. Rating Watch may carry designation – Positive (rating may be raised, negative (lowered), or developing (direction is unclear). A watch should be resolved within foreseeable future, but may continue if underlying circumstances are not settled.

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'.

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, a suspended 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, or e) the entity/issuer defaults.