



The Pakistan Credit Rating Agency Limited

Rating Report

The Bank of Punjab | TFC II | TBI

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Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
27-Jun-2018	AA-	-	-	Initial	-
26-Oct-2017	AA-	-	-	Preliminary	-

Rating Rationale and Key Rating Drivers

The ratings reflect the sustained risk profile of Bank of Punjab (BoP) with an appreciable improvement in profitability and asset quality over the last few years which supplemented the equity base. During current year, the bank has recorded commendable uptick in revenue base – both interest earned and income from fee, commission. However, the bank recorded loss for the year on account of providing for certain infected exposures which were previously secured by Letter of Comfort (LoCs) by the sponsor. Hence, the bank’s recorded significant improvement in its coverage ratio. The bank’s bottom-line again turned green in 1QCY18. The bank witnessed reduction in the non-performing loans inherited by the current management. The bank’s Capital Adequacy Ratio (CAR) clocks in at 9.73% at Dec’17 which improved to 10.53% in 1QCY18. Tier-I CAR declined to 7.61% (Dec’16: 9.40%) due to provisioning against NPLs earlier covered under LOCs. The bank enjoys relaxation from the applicable CAR till Jun’18 granted by the State Bank of Pakistan. Timely re-couping the CAR is essential to ratings. The bank envisages growth in advances wherein the criteria is higher margins with sustained risk profile. Meanwhile, expansion in deposit base with low cost focus, while attracting a wide customer range, is on the cards.

The ratings are dependent on the financial risk profile of the bank, mainly emanating from sustenance of capital adequacy and continued healthy profitability trend in line with the management’s plans. Meanwhile, improvement in asset quality and upholding better governance standards remain imperative.

Disclosure

Name of Rated Entity	The Bank of Punjab TFC II TBI
Type of Relationship	Solicited
Purpose of the Rating	Debt Instrument Rating
Applicable Criteria	Methodology Debt Instruments Rating Methodology(Jun-17),Methodology Bank Rating(Jun-17),Rating Methodology Basel III Instruments(Mar-18)
Related Research	Sector Study Commercial Bank(Jun-18)
Rating Analysts	Sehar Fatima sehar.fatima@pacra.com +92-42-35869504 Jhangeer Hanif jhangeer@pacra.com +92-42-35869504

BANK OF PUNJAB (BoP)	
PROFILE	
Established	1989
Major Business	Commercial Banking
Legal Status	Listed
Head Office	Lahore

INDUSTRY
The banking sector has experienced highest growth in terms of advances in 2017 over the last decade. As a consequence, there is mounting pressure on capital adequacy ratio of the banks. The challenge is exacerbated as the internal generation of capital (profits) are witnessing a dip. Some relief on income side is expected with recent uptick in interest rates.

OWNERSHIP

- The Bank of Punjab, established under the BoP Act 1989, is listed on Pakistan Stock Exchange (PSX). The bank operates with network of 536 branches, mainly concentrated in Punjab. The Government of Punjab (GoPb) holds majority stake in BOP (58%), whereas the rest is widely dispersed.

GOVERNANCE & MANAGEMENT

- The control of the bank vests with ten-member Board of Directors, including the President. Six members, including the Chairman, are representing GoPb on the board. Three are independent members representing minority shareholder while the President is an executive member.
- Mr. Naeemuddin Khan, the President of the Bank since Sep'08, has four decades of diversified banking experience and has been associated with reputed international and domestic banks during his career. The senior management consists of seasoned bankers.
- He is backed by a team of experienced professionals, most of whom have long association with the bank.

RISK MANAGEMENT

- As at end-Dec'17, BoP's advances portfolio constitutes 45% of total assets (end-Dec'16: ~44%)
- During CY17, advances (net) witnessed growth of 13% (against 18% of average industry growth)
- The sectoral concentration inclines towards government (~25%), textile and ginning (~19%) and individuals (~12%). Further analysis reveals that 71% lies with the corporate sector, followed by 13% to the commodity financing.
- The Bank's ADR rationalized to 53.2% (end-Dec'16: 58%)
- NPLs-to-Gross advances improved to ~15% (end-Dec'16: ~19%) primarily on account of increase in lending.
- Loan loss coverage ratio improved to 90% (end-Dec'16: 58%) as the bank provided for some significant exposures during the year. Hence, the drag on equity declined to 18.5% (end-Dec'16: 95%).
- The bank's liquidity, in terms of its Liquid Assets-to-Deposits and Borrowings ratio, strengthened on YoY basis, to ~50% at end-Dec'17 (end-Dec'16: 47%), comprising pre-dominantly government securities.

PERFORMANCE

- During CY17, interest earned stood at PKR 34bln (CY16: PKR ~30bln) primarily on account of 22% and 25% growth witnessed in advances and earning assets respectively. Hence, NIMR clocked in at PKR 15.5bln (CY16: PKR 12.2bln), up 27% YoY.
- Non-Markup income recorded a dip mainly on account of decline in gain on sale of investments. However, improved fee, commission and brokerage income (up 26% YoY) is considered a positive. On the provisioning front, the bank has provided for PKR 12.3bln against certain infected exposures previously secured by Letter of Comfort (LoC) from sponsors. Hence, the bank posted loss of PKR 3.3bln (CY16: PKR 4.8bln profit).
- During CY17, asset yield declined to 6.8% (CY16: 7.2%), in line with industry trend. Cost of funds stood at 3.5% (CY16: 3.8%). Hence, the bank's spread stood at 3.3%, marginally declined from last year of 3.4%.

CAPITAL AND FUNDING

- The main source of BoP's funding is its deposit base, constituting around 89% of the total liabilities at end-Dec'17. The bank witnessed a sizeable growth (23%) in its deposit base mainly driven by customer deposits
- As at end-Dec'17 the bank's Capital Adequacy Ratio reduced to 9.73% (below minimum required level) (Dec'16: 12.28%). However, as at end-Mar18, the Capital Adequacy Ratio improved to 10.53% (previous: 9.73%) with the Tier I ratio improving to 8.44% (previously 7.61%). The bank has been given time till Jun'18 to get compliant with SBP's enlisted CAR requirements.

TFC ISSUES

- In 2016, BoP issued term finance certificates in the amount of PKR 2.5bln to raise Tier-II capital. This privately placed, rated, unsecured and subordinated issue was raised to comply with State Bank of Pakistan's (SBP) regulation to maintain the Capital Adequacy Ratio (CAR). The tenor of the instrument is 10 years from the date of issue. Profit is based on 6M-KIBOR plus a spread. The issue carries lock-in and loss absorbency clauses, as per Basel III capital regulations.
- BoP has issued second TFC of amount PKR 4.3bln. The tenor of the instrument is ten years from the date of the issue (April 2018) whereas the profit is based on 6M-KIBOR plus 125 bps per annum. TFC is unsecured and subordinated as to the payment of principal and profit to all other indebtedness of the bank, including deposits and is not redeemable before maturity without prior approval of the SBP. The TFC is structured to redeem 0.02% of the issue amount, per semi-annual period, in first nine years and the remaining issue in two equal; semi-annual installments of 49.82%, in the tenth (10th) year.



BALANCE SHEET	31-Mar-18	31-Dec-17	31-Dec-16	31-Dec-15
	<i>Annual</i>	<i>Annual</i>	<i>Annual</i>	<i>Annual</i>
Earning Assets				
Advances (Net of NPL)	306,619	290,784	238,968	193,272
Debt Instruments	7,770	7,560	4,695	7,098
Total Finances	314,389	298,344	243,664	200,370
Investments	207,743	237,184	194,712	168,610
Others	52,686	28,732	14,646	7,911
	574,818	564,260	453,022	376,891
Non Earning Assets				
Non-Earning Cash	40,097	44,394	36,438	28,905
Deferred Tax	10,524	10,725	6,480	7,906
Net Non-Performing Finances	2,514	2,731	23,434	26,461
Fixed Assets & Others	27,344	27,438	25,840	32,120
	80,479	85,287	92,192	95,392
TOTAL ASSETS	655,296	649,547	545,214	472,284
Interest Bearing Liabilities				
Deposits	569,600	556,281	453,220	374,961
Borrowings	33,457	43,448	44,329	57,236
	603,057	599,730	497,549	432,198
Non Interest Bearing Liabilities	20,653	20,086	19,811	17,408
TOTAL LIABILITIES	623,710	619,815	517,360	449,605
EQUITY (including revaluation surplus)	31,586	29,732	27,855	22,678
Total Liabilities & Equity	655,296	649,547	545,214	472,284

INCOME STATEMENT	31-Mar-18	31-Dec-17	31-Dec-16	31-Dec-15
Interest / Mark up Earned	9,692	34,451	29,674	31,266
Interest / Mark up Expensed	(5,019)	(18,877)	(17,430)	(20,199)
Net Interest / Markup revenue	4,673	15,574	12,244	11,068
Other Income	917	4,591	5,294	7,624
Total Revenue	5,591	20,165	17,539	18,692
Non-Interest / Non-Mark up Expensed	(2,761)	(10,646)	(8,464)	(7,666)
Pre-provision operating profit	2,830	9,519	9,075	11,026
Provisions	179	(14,217)	(1,025)	(3,496)
Pre-tax profit	3,009	(4,698)	8,050	7,529
Taxes	(1,069)	1,376	(3,192)	(2,781)
Net Income	1,940	(3,322)	4,858	4,748

Ratio Analysis	31-Mar-18	31-Dec-17	31-Dec-16	31-Dec-15
Performance				
ROE	27.9%	13.0%	22.3%	27.4%
Cost-to-Total Net Revenue	54.5%	58.1%	53.3%	44.9%
Provision Expense / Pre Provision Profit	-6.3%	149.4%	11.3%	31.7%
Capital Adequacy				
Equity/Total Assets	4.4%	4.1%	4.4%	4.1%
Capital Adequacy Ratio as per SBP	10.5%	9.7%	12.3%	10.5%
Funding & Liquidity				
Liquid Assets / Deposits and Borrowings	48.0%	49.5%	47.0%	41.9%
Advances / Deposits	54.7%	53.2%	57.8%	58.5%
CASA deposits / Total Customer Deposits	70.4%	71.4%	71.0%	65.9%
Intermediation Efficiency				
Asset Yield	6.8%	6.8%	7.2%	8.9%
Cost of Funds	3.4%	3.5%	3.8%	5.0%
Spread	3.5%	3.3%	3.4%	3.9%



Bank of Punjab
TFC Specifications

Nature of Instrument	Size of Issue (PKR mln)	Tenor (yrs)	Security	Trustee
TFC I	PKR 2,500mln	10	Unsecured, subordinated as to the payment of principal and profit to all other indebtedness of the Bank, including deposits, and will not be redeemable before maturity without prior approval of SBP. Also subject to lock-in and loss absorbency clauses.	Pak Brunei Investment Company Limited

Nature of Instrument	Size of Issue (PKR mln)	Tenor (yrs) & Principal Redemption	Security	Trustee
TFC II	PKR 4,300mln	10 years, Two equal, semi-annual installments of 49.82% in tenth year	Unsecured, subordinated as to the payment of principal and profit to all other indebtedness of the Bank, including deposits, and will not be redeemable before maturity without prior approval of SBP. Profit is based on 6M-KIBOR plus 125 bps p.a. Also subject to lock-in and loss absorbency clauses.	Pak Brunei Investment Company Limited

DEBT INSTRUMENT RATING SCALE & DEFINITIONS

The instrument rating reflects forward-looking opinion on credit worthiness of underlying debt 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		SHORT TERM RATINGS	
AAA	Highest credit quality. Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments.	<p>A1+: The highest capacity for timely repayment.</p> <p>A1: A strong capacity for timely repayment.</p> <p>A2: A satisfactory capacity for timely repayment. This may be susceptible to adverse changes in business, economic, or financial conditions.</p> <p>A3: An adequate capacity for timely repayment. Such capacity is susceptible to adverse changes in business, economic, or financial conditions.</p> <p>B: The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions.</p> <p>C: An inadequate capacity to ensure timely repayment.</p>	
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.		

<p>Outlook (Stable, Positive, Negative, Developing)</p> <p>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’.</p>	<p>Rating Watch</p> <p>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.</p>	<p>Suspension</p> <p>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.</p>	<p>Withdrawn</p> <p>A rating is withdrawn on a) termination of rating mandate, b) the debt instrument is redeemed, c) the rating remains suspended for six months, d) the entity/issuer defaults., or/and e) PACRA finds it impractical to surveil the opinion due to lack of requisite information</p>
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- iii. The analyst is not a substantial shareholder of the customer being rated by PACRA [Annexure F; d-(ii)] Explanation: for the purpose of above clause, the term “family members” shall include only those family members who are dependent on the analyst and members of the rating committee

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- (7) PACRA uses due care in preparation of this Rating Report. Our information has been obtained from sources we consider to be reliable but its accuracy or completeness is not guaranteed. PACRA does not, in every instance, independently verifies or validates information received in the rating process or in preparing this Rating Report.
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