The Pakistan Credit Rating Agency Limited

Rating Report

AlBaraka Bank (Pakistan) Limited

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Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
29-Jun-2018	A	A1	Stable		-
29-Dec-2017	A	A1	Positive	Maintain	-
30-Jun-2017	A	A1	Positive	Maintain	-
22-Sep-2016	A	A1	Developing	Rating Watch	-
25-Jun-2016	A	A1	Stable	Maintain	-

Rating Rationale and Key Rating Drivers

The ratings reflect ABPL's association with AlBaraka Banking Group – a strong Middle Eastern banking institution. ABPL witnessed improvement in net spread on account of lower cost of deposit as ABPL shed high-cost deposits and enhanced contribution of CASA. A sizeable book of GoP securities in the investment portfolio helped maintaining adequate liquidity. Going forward, the management aims low cost deposit mix and cautious credit growth, in turn, better profits. Success in planned initiatives is crucial.

Effective implementation of business strategy, particularly in the back drop of challenging operating environment and competitive banking landscape, is important. Pivotal to this strategy is achieving profitability and hence generation of internal capital. As at Mar-18, overall CAR of the Bank is reported at 10.02% which is below the regulatory requirement, and to address this sponsors are willing to inject $20mln as ADT-I, modality of which is in approval stage. This is expected to provide breathing space to the Bank. Moreover, improving diversification in revenue streams, particularly from non-fund based avenues and maintaining healthy asset quality are important for bottom-line performance.

Disclosure

Name of Rated Entity	AlBaraka Bank (Pakistan) Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology | Bank Rating(Jun-17)
Related Research	Sector Study | Commercial Bank(Jun-18)
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ALBARAKA BANK PAKISTAN LIMITED PROFILE	
Incorporated	1991
Major Business	Commercial Bank
Legal Status	Unlisted
Head Office	Karachi

PROFILE AND OWNERSHIP

- AlBaraka Islamic Bank B.S.C. (c) (ABIB), through its Pakistan branches started its operations in Pakistan in 1991. However, after acquisition of ~50% shares of Emirates Global Islamic Bank Limited (EGIBL) by ABIB, Pakistan Branches of ABIB were merged with and into EGIBL during October 2010 to form ABPL.
- ABPL operates through a network of 188 branches as at end-Dec 17.
- Major shareholders of ABPL are ABIB (~59%), Islamic Corporation for the development of the Private Sector (ICD) (12%), Mal Al Khaleej group (~12%), Sheikh Tariq Bin Faisal Khalid Al Qassem (~8%) and Mr. Muhammad Umar Ijaz (3%).

GOVERNANCE AND MANAGEMENT

- The overall control of the Bank vests in the ten-member Board of Directors (BoD).
- Four Board members represent AlBaraka Banking Group, and one each from Islamic Corporation for the development of the Private Sector (ICD) and Mal Al Khaleej Investments LLC, whereas the other four board members are independent. Mr. Adnan Ahmed Yousif, CEO ABG, is the Chairman of the Board.
- Mr. Ahmed Shuja Kidwai; CEO ABPL is a professional banker with many decades of experience.

RISK MANAGEMENT

- Advances exhibited a growth of 6% which is considerably below the industry's average of 19% (CY16: 15%).
- Post-merger ABPL NPLs increased to PKR 7bln although majority is provided. NPLs to gross advances ratio remained stagnant (CY17: 10%, CY16: 10%). Infection ratio decreased to 9.6% during Q1CY18 (CY17: 10.1%).
- Owing to a shrinking deposit base, ADR increased to 72% in CY17 (CY16: 63%).
- Advances' concentration in terms of top-20 slightly decreased to 24% (CY16: 25%).

BUSINESS & FINANCIAL RISK

- ABPL's asset yield increased in CY17, through efficient cost management as low cost deposits helped bank to earn an average spread of 4.3% (CY16: 3.6%).
- The net revenue increased by a whopping 54% (CY17: 3.6bln, CY16 2.3bln).
- The cost to total net revenue ratio increased to 112% (CY16: 108%). ABPL hit a bottom line loss of PKR 389mln (CY15: PKR -156mln).
- During 1QCY18, owing higher earning assets and increasing profit rates, ABPL's net revenue experienced an increase. This resulted in pre-provision profit of PKR 23mln. However, provisioning expense of PKR 370mln translated in to a loss of PKR 221mln.

FINANCIAL RISK

- The bank's liquidity position evident by Liquid assets to Deposits & Borrowing ratio (1QCY18: 29%; CY17: 31%; CY16: 44%) declined on a YoY basis owing to decreasing liquid assets.
- Unlike growth in the industry deposit base, ABPL did not witness expansion on its deposit side.
- The deposit mix of ABPL, in terms of CASA as percentage of total customer deposits, has increased to 80% (Dec16: 75%) as the Bank continued to shed high-cost term deposits and mobilized low cost savings deposits.
- The top 20 depositors' concentration has been increasing in the recent years (end-Dec17: 19%; end-Dec16: 18%).

CAPITAL RISK

- Bank's CAR stands at 10.2% as at end-Dec17 (Dec16: 10.3%), which is below the regulatory requirement.
- In order to meet the increasing regulatory requirement of CAR, ABG is willing to inject \$20mln, modality of which is in approval stage.
- This injection of ADT1 would somewhat relieve pressure from the current CAR of 10.2 as at end-Dec17 but meeting further SBP requirements of minimum 11.9% CAR till end-Dec18 and 12.5% till end-Dec19 with constrained bottom-line would become increasingly difficult.

The Pakistan Credit Rating Agency Limited

AlBaraka Bank (Pakistan) Limited

BALANCE SHEET	31-Mar-18	31-Dec-17	31-Dec-16	31-Dec-15
	3MCY18	CY17	CY16	CY15
Earning Assets				
Advances	69,314	67,841	63,944	46,506
Debt Instruments	2,987	2,514	2,227	1,192
Total Finances	72,301	70,355	66,171	47,697
Investments	16,723	16,879	22,375	16,166
Others	5,386	8,028	3,677	3,392
	94,410	**95,262**	**92,223**	**67,256**
Non Earning Assets				
Non-Earning Cash	8,462	8,916	18,725	10,847
Deferred Tax	3,405	3,239	2,873	1,392
Net Non-Performing Finances	2,698	3,362	2,841	1,139
Fixed Assets & Others	9,808	9,882	10,137	6,298
	24,373	**25,399**	**34,576**	**19,676**
TOTAL ASSETS	**118,783**	**120,661**	**126,799**	**86,932**
Interest Bearning Liabilities				
Deposits	96,974	98,590	105,843	71,644
Borrowings	6,094	5,852	4,652	5,865
	103,069	104,442	110,495	77,509
Non Interest Bearing Liabilities	5,202	5,456	4,914	3,150
TOTAL LIABILITIES	**108,271**	**109,898**	**115,409**	**80,659**
EQUITY (including revaluation surplus)	**10,513**	**10,762**	**11,390**	**6,273**
Total Liabilities & Equity	**118,783**	**120,661**	**126,799**	**86,932**

INCOME STATEMENT	31-Mar-18	31-Dec-17	31-Dec-16	31-Dec-15
	3MCY18	CY17	CY16	CY15
Profit / Return Earned	1,739	6,718	5,158	6,269
Return Expensed	(797)	(3,078)	(2,795)	(3,791)
Net Revenue	**942**	**3,640**	**2,363**	**2,478**
Other Income	266	967	874	656
Total Revenue	**1,208**	**4,607**	**3,237**	**3,135**
Admin and Other Expenses	(1,185)	(5,040)	(3,502)	(2,854)
Pre-provision Operating Profit	23	(433)	(265)	281
Provisions	(370)	(98)	164	125
Pre-tax profit	(347)	(531)	(101)	407
Taxes	126	142	(55)	(166)
Net Income / (Loss)	**(221)**	**(389)**	**(156)**	**240**

Ratio Analysis	31-Mar-18	31-Dec-17	31-Dec-16	31-Dec-15
	3MCY18	CY17	CY16	CY15
Performance				
ROE	-8.3%	-3.5%	-1.8%	3.9%
Cost-to-Total Net Revenue	98.1%	111.6%	108.3%	91.6%
Provision Expense / Pre Provision Profit	1608.7%	-22.7%	62.0%	-44.6%
Capital Adequacy				
Equity/Total Assets	8.7%	8.8%	8.7%	7.2%
Capital Adequacy Ratio as per SBP	10.0%	10.2%	10.3%	14.5%
Funding & Liquidity				
Liquid Assets / Deposits and Borrowings	28.6%	31.4%	43.6%	38.9%
Advances / Deposits	74.0%	72.2%	63.1%	66.5%
CASA deposits / Total Customer Deposits	80.2%	80.1%	74.7%	75.3%
Intermediation Efficiency *				
Asset Yield	7.4%	7.2%	6.6%	8.6%
Cost of Funds	3.1%	2.9%	3.0%	4.6%
Spread	4.3%	4.3%	3.6%	4.0%
Outreach				
Branches	188	188	224	135

** Mar18 numbers have been calculated with comparatives of Mar17*

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

Rating Team Statements
(1) Rating is just an opinion about the creditworthiness of the entity and does not constitute recommendation to buy, hold or sell any security of the entity rated or to buy, hold or sell the security rated, as the case may be | Chapter III; 14-3-(x)

2) **Conflict of Interest**
i. The Rating Team or any of their family members have no interest in this rating | Chapter III; 12-2-(j)
ii. PACRA, the analysts involved in the rating process and members of its rating committee, and their family members, do not have any conflict of interest relating to the rating done by them | Chapter III; 12-2-(e) & (k)
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

Restrictions
(3) No director, officer or employee of PACRA communicates the information, acquired by him for use for rating purposes, to any other person except where required under law to do so. | Chapter III; 10-(5)
(4) PACRA does not disclose or discuss with outside parties or make improper use of the non-public information which has come to its knowledge during business relationship with the customer | Chapter III; 10-7-(d)
(5) PACRA does not make proposals or recommendations regarding the activities of rated entities that could impact a credit rating of entity subject to rating | Chapter III; 10-7-(k)

Conduct of Business
(6) PACRA fulfills its obligations in a fair, efficient, transparent and ethical manner and renders high standards of services in performing its functions and obligations; | Chapter III; 11-A-(a)
(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.
(8) PACRA prohibits its employees and analysts from soliciting money, gifts or favors from anyone with whom PACRA conducts business | Chapter III; 11-A-(q)
(9) PACRA ensures before commencement of the rating process that an analyst or employee has not had a recent employment or other significant business or personal relationship with the rated entity that may cause or may be perceived as causing a conflict of interest; | Chapter III; 11-A-(r)
(10) PACRA maintains principal of integrity in seeking rating business | Chapter III; 11-A-(u)
(11) PACRA promptly investigates, in the event of a misconduct or a breach of the policies, procedures and controls, and takes appropriate steps to rectify any weaknesses to prevent any recurrence along with suitable punitive action against the responsible employee(s) | Chapter III; 11-B-(m)

Independence & Conflict of interest
(12) PACRA receives compensation from the entity being rated or any third party for the rating services it offers. The receipt of this compensation has no influence on PACRA´s opinions or other analytical processes. In all instances, PACRA is committed to preserving the objectivity, integrity and independence of its ratings. Our relationship is governed by two distinct mandates i) rating mandate - signed with the entity being rated or issuer of the debt instrument, and fee mandate - signed with the payer, which can be different from the entity
(13) PACRA does not provide consultancy/advisory services or other services to any of its customers or to any of its customers' associated companies and associated undertakings that is being rated or has been rated by it during the preceding three years unless it has adequate mechanism in place ensuring that provision of such services does not lead to a conflict of interest situation with its rating activities; | Chapter III; 12-2-(d)
(14) PACRA discloses that no shareholder directly or indirectly holding 10% or more of the share capital of PACRA also holds directly or indirectly 10% or more of the share capital of the entity which is subject to rating or the entity which issued the instrument subject to rating by PACRA; | Reference Chapter III; 12-2-(f)
(15) PACRA ensures that the rating assigned to an entity or instrument is not be affected by the existence of a business relationship between PACRA and the entity or any other party, or the non-existence of such a relationship | Chapter III; 12-2-(i)
(16) PACRA ensures that the analysts or any of their family members shall not buy or sell or engage in any transaction in any security which falls in the analyst's area of primary analytical responsibility. This clause shall, however, not be applicable on investment in securities through collective investment schemes. | Chapter III; 12-2-(l)
(17) PACRA has established policies and procedure governing investments and trading in securities by its employees and for monitoring the same to prevent insider trading, market manipulation or any other market abuse | Chapter III; 11-B-(g)

Monitoring and review
(18) PACRA monitors all the outstanding ratings continuously and any potential change therein due to any event associated with the issuer, the security arrangement, the industry etc., is disseminated to the market, immediately and in effective manner, after appropriate consultation with the entity/issuer; | Chapter III | 18-(a)
(19) PACRA reviews all the outstanding ratings on semi-annual basis or as and when required by any creditor or upon the occurrence of such an event which requires to do so; | Chapter III | 18-(b)
(20) PACRA initiates immediate review of the outstanding rating upon becoming aware of any information that may reasonably be expected to result in downgrading of the rating; | Chapter III | 18-(c)
(21) PACRA engages with the issuer and the debt securities trustee, to remain updated on all information pertaining to the rating of the entity/instrument; | Chapter III | 18-(d)
Probability of Default
(22) PACRA´s Rating Scale reflects the expectation of credit risk. The highest rating has the lowest relative likelihood of default (i.e, probability). PACRA´s transition studies capture the historical performance behavior of a specific rating notch. Transition behavior of the assigned rating can be obtained from PACRA´s Transition Study available at our website. (www.pacra.com). However, actual transition of rating may not follow the pattern observed in the past | Chapter III | 14-(f-VII)
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