



The Pakistan Credit Rating Agency Limited

Rating Report

BankIslami Pakistan Limited

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Rating History					
Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
08-Oct-2019	A+	A1	Stable	Maintain	-
30-Apr-2019	A+	A1	Stable	Maintain	YES
27-Dec-2018	A+	A1	Stable	Maintain	YES
22-Jun-2018	A+	A1	Stable	Maintain	-
13-Dec-2017	A+	A1	Developing	Maintain	YES
22-Jun-2017	A+	A1	Developing	Maintain	-
25-Oct-2016	A+	A1	Rating Watch- Developing	Maintain	-
06-May-2016	A+	A1	Developing	Rating Watch	-
08-May-2015	A+	A1	Stable	RW-Developing	-
24-Apr-2015	A+	A1	Stable	Upgrade	-
30-Jun-2014	A	A1	Positive	Maintain	-

Rating Rationale and Key Rating Drivers

The ratings reflect BankIslami's sustained risk profile. During 1HCY19, the bank's profit increased owing to asset yield driven by increase in policy rate and earning assets. The bank's new management is emphatically pursuing for recovery of NPLs. In 1HCY19, NPLs inched down on account of some recoveries. The funding base comprise of deposits and borrowings. The bank witnessed slight uptick in its asset yield, better than the cost - ultimately translating into better spread. Deposit mix (CASA) and concentration need to improve. The bank was able to achieve good operating profits; trend should continue. Key positions are headed by experienced individuals. The bank's management is positive about performance and achieving cost efficiency, pursuing the new business plan under leadership of the CEO. The focus is on risk management, IT infrastructure, workforce strengthening and customer facilitation which will help bank to achieve operational efficiency. The bank has taken steps to strengthen its fortress against cyber risks; adequate provision has been created. Going forward, primary focus is to consolidate CAR as the relaxations given by central bank will be withdrawn in CY21. The management is following the planned steps to enhance capital of the bank which will assist in inching up CAR.

The bank's ability to raise its capital base in order to pursue its growth plan is important. In this regard, BIPL's Board is raising the bank's equity approximately by Rs. 1 billion. It has also approved the issuance of Sukuk of worth Rs. 2 billion which will add to Additional Tier-1 Sukuk of the bank. Additionally, the bank's operational profitability needs to be observed against financial ramifications which may emanate from recent cyber attack or incidence due to non-performing assets owing to slow economic growth.

Disclosure	
Name of Rated Entity	BankIslami Pakistan Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	PACRA_Methodology_FI_FY19(Jun-19),PACRA_Methodology_DI Basel III_FY19(Jun-19),PACRA_Methodology_Sukuk_FY19(Jun-19)
Related Research	Sector Study Commercial Bank(Jun-19)
Rating Analysts	Usama Zubair usama.zubair@pacra.com +92-42-35869504

**Profile**

Structure BankIslami Pakistan Limited (BIPL), incorporated in Oct-04, was the first bank in Pakistan to receive the Islamic Banking license, in Mar-05, under the Islamic Banking Policy of 2003. The bank, after being declared a scheduled Islamic bank by the State Bank of Pakistan in Mar-05, commenced its operations from April 07, 2006.

Background The bank has been following organic growth since its inception. Furthermore, on May 7th, 2015, BIPL acquired defunct bank "KASB Bank Limited" under "Scheme of amalgamation of defunct KASB Bank Limited with and into BankIslami Pakistan Limited under Section 47 of Banking Companies Ordinance, 1962".

Operations BankIslami is operating as Scheduled Islamic Commercial Bank. It's a small sized Islamic bank with a network of 330 branches.

Ownership

Ownership Structure BIPL has four prominent sponsors namely JS Group (through Jahangir Siddiqui & Company Limited (JSCL), Mr. Ali Hussain and SAJ Capital Management Limited, Emirates NBD (through Dubai Bank PJSC), and Randeree family. All these have a collective holding of ~76% in the bank and predominantly direct the affairs of the BIPL's board.

Stability BIPL ownership is backed by strong sponsors and has been same for many years. It is expected to remain same in the foreseeable future.

Business Acumen All sponsors are renowned business groups with stakes in various sectors with national and international presence. The business acumen of sponsors is considered strong as sponsors have diversified interest and long association with the markets.

Financial Strength The ability to support in case of financial need is considered good.

Governance

Board Structure BIPL's eight member board of directors (BoD) including CEO constitutes representatives of sponsoring groups. Currently, one from DCD group, two are independent directors, five are non-executive (including DCD representation) and one Executive director (CEO - Bank Islami). BIPL's shariah board comprises three leading Islamic scholars for the country, namely (i) Mufti Irshad Ahmad Aijaz, ii) Mufti Muhammad Husain, and iii) Mufti Javed Ahmed.

Members' Profile Mr. Ali Hussain, MD SAJ Capital Limited, is the Chairman of the Board, has ~38 years of experience. All the other board members have different educational and work experience background.

Board Effectiveness The BoD exercises close monitoring of the management's policies and governs the bank's operations through its six committees namely i) Audit Committee, ii) Board Remuneration Committee iii) Human Resource & Management Committee, (iv) Risk Management Committee, (v) IT Committee and (vi) Executive Committee. IT committee is a new addition.

Financial Transparency During the year, EY Ford Rhodes Chartered Accountants the external auditor are SBP panel member, expressed an unqualified opinion for the financial statements for the year ending December 31st, 2018 and performed interim review for six months ending June, 2019. Besides this, they have identified the key matters which are significant in respect of audit.

Management

Organizational Structure BIPL's organizational structure is divided into twelve functional departments i) Distribution, ii) Corporate Banking, iii) Consumer, iv) Treasury/ FIs, v) Risk Management, vi) Product and Shariah Structuring, vii) Human Resource, viii) Legal, ix) Finance, x) Operations, xi) Security and Govt. Relations and xii) Compliance.

Management Team Mr. Syed Amir Ali has joined the bank as Deputy CEO in Apr-18. He has taken up the position of 'President & CEO' in Oct-18. He is a Chartered Accountant & CFA Charter holder by qualification, carrying with himself more than one decade experience mainly of Meezan Bank. The BIPL is focusing on the improvement of team efficiency.

Effectiveness The bank has nine committees at the management level: (i) Business Review Committee (BRC), (ii) IT Steering Committee (ITSC), (iii) Asset & Liability Committee (ALCO), (iv) Compliance & Controls Committee (CCM), (v) Service Excellence Committee (SEC), (vi) Management Credit Committee (MCC), (vii) Disciplinary Action Committee (DAC), (viii) Management Team Committee (MANCOM), and (ix) Procurement & Disposal Committee (PDC).

MIS The management has selected a comprehensive Islamic Banking application that has inbuilt Shariah compliance features – iMal, a core banking software, which has been developed by Path Solutions, a software house in the Middle East.

Risk Management Framework Risk Rating Module Vista Plus is being used by the bank. The module supports the bank in its internal Obligor Risk Rating (ORR) process by adding more objectivity to the credit appraisal process.

Business Risk

Industry Dynamics The banking industry witnessed expansion in the loan and deposit book by 23.7% and 10.7% respectively. Last year and YTD (2018) both witnessed huge deployments. This is expected to slow down. New projects require gestation period and additionally crowding-out effect may take place. Rising interest rates mean profitability of the sector would take support. Yet NPLs, as a result, may also transpire. CAR is reaching the maximum requirement by December 2019 (12.5%). This will create a challenge for some of the players.

Relative Position The BIPL is small tier bank and was able to maintain its deposit system share of 1.3% (Dec-17: 1.3%).

Revenues During period 6M CY19, the bank earned mark-up of PKR 9.8bln (6M18: PKR 5.6bln; CY18: PKR 7.2bln). The increase of 75% YoY is due to the earnings from consolidation in advances book and new investments in sovereign guaranteed papers. The bank recorded NIMR at PKR 4.8bln (6M18: PKR 2.7bln), up only by 78% YoY. As at end-Jun19, bank's asset yield increased which led to improvement in spread which stood at 6.3% (end-Dec18: 3.8%) - a positive factor.

Performance Other operating income of the bank inched down to stand at PKR 523mln (6M CY18: PKR 560mln) primarily due to decline in fee, commission income. Other operating expenses inched up to PKR 3.6bln (6M CY18: PKR 3.2bln), up 12.5% YoY. Net provisions of PKR 894mln further dwindle the profit before tax to PKR 895mln. Furthermore, tax expense increased to PKR 314mln (6M CY18: PKR 29mln). Hence, profit after tax stood at PKR 581mln (6M CY18: PKR 65mln).

Sustainability Going forward, the bank aims to expand its lending portfolio by funding through low cost deposits. The bank is prioritizing the rated client lending in future which will assist in CAR measures. Recovery from non-performing loans transferred from KASB is also a priority. Going forward, risk management framework improvement will be focused by the bank.

Financial Risk

Credit Risk The bank NPL's decreased to PKR 12.8bln as at end-Jun19 (end-Dec18: PKR 15.4bln) as some NPLs were settled or restructured, which led to decline in NPLs to Gross Advances ratio (end-Jun19: 11.0%; end-Dec18: 11.9%). Further, drag on equity (Net NPLs/Equity: end-Jun19: 10.3%; end-Dec18: 33.5%) is reduced.

Market Risk BIPL's investment portfolio increased to PKR 56.2bln (end-Dec18: PKR 38.8bln) primarily funded by deposits. Portfolio increased mainly due to investment in Pakistan Energy Sukuk of PKR 35mln; sovereign guaranteed Sukuk. The investment composition remained tilted towards government securities (end-Jun19: 83%; end-Jun18: 92%), excluding debt instruments.

Liquidity And Funding As at end-Jun19, BIPL's customer deposits increased to PKR 201bln (end-Dec18: PKR 174.7bln), up 15% owing to greater increase witnessed in time deposits. CA and SA ratios decline slightly (end-Jun19: 33%; end-Jun18: 38%) & (end-Jun19: 29%; end-Jun18: 36%) respectively, which may increase cost of funding in the upcoming year. The bank's liquidity position has significantly increased evident by Liquid assets to Deposits & Borrowing ratio (end-Jun19: 30.4%; end-Dec18: 20.4%), primarily driven by the increase in government securities.

Capitalization The bank has equity base of PKR 13.2bln whereby the same goes up to PKR 15bln when surplus on revaluation is added. At end-Jun19, CAR is largely maintained at 15.4% with Tier I at 11.2%. Currently, the bank is issuing Additional Tier-I Sukuk of PKR 2.0bln (including green shoe option of PKR 500mln) to support Tier-I capital in the future.



BankIslami Pakistan Limited

PKR mln

BALANCE SHEET	30-Jun-19 6M	31-Dec-18 CY18	31-Dec-17 CY17	31-Dec-16 CY16
Earning Assets				
Advances	117,240	114,331	114,992	75,415
Debt Instruments	9,223	9,769	5,240	1,018
Total Finances	126,463	124,100	120,232	76,433
Investments	47,364	28,787	36,543	45,300
Others	23,593	19,006	22,174	28,359
	197,420	171,893	178,949	150,091
Non Earning Assets				
Non-Earning Cash	21,420	14,293	11,784	8,921
Deferred Tax	7,372	7,530	7,702	5,918
Net Non-Performing Finances	472	4,516	4,472	2,402
Fixed Assets & Others	27,473	17,511	14,886	15,141
	56,738	43,850	38,844	32,383
TOTAL ASSETS	254,159	215,743	217,792	182,473
Interest Bearing Liabilities				
Deposits	213,941	184,693	178,310	153,736
Borrowings	8,305	7,820	15,570	6,066
	222,247	192,513	193,880	159,802
Non Interest Bearing Liabilities	16,817	8,716	10,236	10,227
TOTAL LIABILITIES	239,064	201,228	204,116	170,029
EQUITY (including revaluation surplus)	15,095	14,515	13,676	12,445
TOTAL LIABILITIES & EQUITY	254,159	215,743	217,792	182,473

INCOME STATEMENT	30-Jun-19 6M	31-Dec-18 CY18	31-Dec-17 CY17	31-Dec-16 CY16
Profit / Return Earned	9,865	12,204	10,354	10,128
Return Expensed	(5,002)	(6,170)	(5,250)	(5,791)
NIMR	4,864	6,034	5,104	4,336
Other Income	523	1,264	965	638
Total Revenue	5,387	7,298	6,069	4,974
Other Expenses	(3,598)	(6,859)	(6,303)	(6,160)
Pre-provision operating profit	1,789	439	(235)	(1,186)
(Provisions)/ Reversal	(894)	(37)	392	2,030
Pre-tax profit / (Loss)	895	403	157	844
Taxes	(314)	(190)	1,406	(391)
Net Income/ (Loss)	581	213	1,563	452

RATIO ANALYSIS	30-Jun-19 6M	31-Dec-18 CY18	31-Dec-17 CY17	31-Dec-16 CY16
Performance				
ROE	4.5%	1.7%	13.5%	4.3%
Cost-to-Total Net Revenue	67.6%	95.1%	105.2%	126.7%
Provision Expense / Pre Provision Profit	50.0%	8.4%	167.1%	171.1%
Capital Adequacy				
Equity/Total Assets	5.2%	5.9%	5.7%	5.9%
Capital Adequacy Ratio as per SBP	15.4%	15.1%	14.5%	13.4%
Funding & Liquidity				
Liquid Assets / Deposits and Borrowings	30.4%	20.4%	23.5%	32.7%
Advances / Deposits	55.2%	64.2%	66.8%	50.4%
CASA deposits / Total Customer Deposits	61.9%	68.6%	73.0%	70.2%
Intermediation Efficiency				
Asset Yield	10.7%	7.0%	6.3%	7.0%
Cost of Funds	4.8%	3.2%	3.0%	3.7%
Spread	5.9%	3.8%	3.4%	3.3%
Outreach				
Branches	330	330	330	321

Annualized*

BankIslami Pakistan Limited

Sep-19

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		Short Term Ratings	
AAA	Highest credit quality. Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments	A1+	The highest capacity for timely repayment.
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.	A1	A strong capacity for timely repayment.
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.	A2	A satisfactory capacity for timely repayment. This may be susceptible to adverse changes in business, economic, or financial 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.	A3	An adequate capacity for timely repayment. Such capacity is susceptible to adverse changes in business, economic, or financial conditions.
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	The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions.
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.	C	An inadequate capacity to ensure timely repayment.
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.		



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 surveil the opinion due to lack of requisite information.

Harmonization A change in rating due to revision in applicable methodology or underlying scale.

Disclaimer: PACRA’s ratings are an assessment of the credit standing of entities/issue in Pakistan. They do not take into account the potential transfer / convertibility risk that may exist for foreign currency creditors. PACRA’s opinion is not a recommendation to purchase, sell or hold a security, in as much as it does not comment on the security’s market price or suitability for a particular investor.

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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