



The Pakistan Credit Rating Agency Limited

Rating Report

Bank Alfalah Limited | TFC V | Feb-13

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Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
28-Dec-2018	AA	-	Stable	Maintain	-
14-Jun-2018	AA	-	Stable	Maintain	-
29-Dec-2017	AA	-	Stable	Maintain	-
22-Jun-2017	AA	-	Stable	Upgrade	-
30-Jun-2016	AA-	-	Positive	Maintain	-

Rating Rationale and Key Rating Drivers

The ratings reflect relative positioning of the bank among large banks of the country. The bank has a stronger position in advances - sustained by fresh deployments. BAFL embarked upon a strategy to sustainably rationalize its cost of funding with enduring focus on low cost deposits. Resultantly, BAFL's cost of fund is comparable to some of the large banks. The bank enjoys extended outreach across the country which has augmented its deposit base. Operating cost structure has improved on YoY basis on account of cost rationalization. The asset quality of the bank has sustained over the past three years on account of prudent risk management. Effective implementation of the envisaged business strategy is important. The increasing asset yield and cost efficiency enabled spreads to increase slightly. The bank issued Tier-I instrument to improve its capital, whereas, enhancing Tier-II capital through issue of a new instrument is also an option, which the bank can continue to avail from time to time.

The ratings are dependent on the improved positioning of the bank. Improvement in spreads is essential to profitability. Strengthening of the bank's capitalization backed by strong sponsors support and adding granularity to its advances and deposits book are essential.

Disclosure

Name of Rated Entity	Bank Alfalah Limited TFC V Feb-13
Type of Relationship	Solicited
Purpose of the Rating	Debt Instrument Rating
Applicable Criteria	Methodology Financial Institution(Jun-18),Methodology Basel III Compliant - Debt Instrument(Jun-18)
Related Research	Sector Study Commercial Bank(Jun-18)
Rating Analysts	Muhammad Obaid muhammad.obaid@pacra.com +92-42-35869504



Profile

Structure Bank Alfalah Limited (hereinafter referred as “BAFL” or “the bank”) was incorporated as a public limited company, in 1992, and is listed on Pakistan Stock Exchange (PSX).

Background Bank commenced operations in 1992. Since its inception, Bank Alfalah has grown rapidly to become Pakistan’s one of the largest private bank, the largest issuer and acquirer of credit cards, and one of the largest Islamic Banking businesses in the country. The Bank has a network of 640 branches spanning in more than 200 cities in Pakistan and a presence in Afghanistan, Bangladesh, Bahrain and the UAE.

Operations Bank provides financial solutions to consumers, corporations, institutions and governments through a broad spectrum of products and services, including corporate and investment banking, consumer banking and credit, commercial, SME, agri-finance, Islamic and asset financing. The Bank currently serves more than 1.7 million customers.

Ownership

Ownership Structure BAFL is majority owned by the Abu Dhabi Group (ADG) (50.23%), rest is owned by IFC (14.76%), Mutual funds and other NBFIs (26.18%) and General public (8.82%) at Sep18 end.

Stability HR committee designs succession planning policies for the CEO and Key executives. Internal successors were highlighted in addition to earmarking key potential external resources to ensure a robust pipeline across all levels at the Bank.

Business Acumen ADG consists of some of the prominent members of UAE’s ruling family and leading businessmen of UAE. ADG, being a distinguished business group, maintains substantial presence in the country’s financial sector, and strong foothold in telecommunication sector.

Financial Strength Sponsors, being ruling family of UAE, possess strong financial ability to support BAFL in case of need. Furthermore, direct and indirect business interests of the sponsor group is spread throughout various industry sectors including banking, telecom, insurance, project financing and investment management.

Governance

Board Structure Subsequent to the elections of BAFL directors, held in May 18, the board comprises of nine members including President/CEO and eight non-executive directors, four of whom are representatives of ADG, one is an IFC nominee, while three members are independent.

Members’ Profile Chairman of the board, H.H. Sheikh Nahayan Mubarak Al Nahayan, is a well-known and seasoned businessman having direct and indirect business interests through various industry sectors in numerous countries.

Board Effectiveness The board actively participates in strategy formulation and effectively monitors the managerial affairs of the bank. The BoD has constituted six committees to ensure rigorous monitoring of the management’s policies and bank’s operations.

Financial Transparency M/s. EY Ford Rhodes, Chartered Accountants, expressed an unmodified conclusion vide their review report for the half year ended June 30, 2018. The retiring auditors M/s KPMG Taseer Hadi & Co., Chartered Accountants, completed the period of five years and therefore, were not eligible for re-appointment. Further, an independent and objective internal audit function is in place covering all activities of the bank with emphasis on risk management and internal controls.

Management

Organizational Structure A well-defined organizational structure exists. Operations are segregated into various departments wherein clear lines of responsibility are defined for each cadre.

Management Team BAFL’s senior management team comprises experienced bankers having national and international exposure. Nauman Ansari, CEO, is reputed to be a seasoned banker with strong professional acumen with 24 year professional career in commercial banking.

Effectiveness The bank has formulated two key management committees, Central Management Committee (CMC) and Central Credit Committee (CCC). These committees are headed by the President and include senior executives. Furthermore, BAFL has various sub-committees of CMC, with defined areas of oversight. Functions of the management committees are clear and well-defined to effectively achieve its underlying goals and objectives.

MIS The bank uses Temenos (T-24) as its core banking software across all branches. With implementation of T-24 and other support systems, all banking processes conducted across the entire branch network of the bank, have been centralized resulting in manifold benefits like extended control, time efficiency, reduction in staff costs, and improved MIS.

Risk Management Framework Bank has a framework for effective identification, measurement, monitoring, integration and management of different financial and non-financial risks that are constantly evolving as business activities change in response to concurrent internal and external developments. The Board Risk Management Committee (BRMC) is appointed to assist in design, regular evaluation and timely updating of the risk management framework of the Bank.

Business Risk

Industry Dynamics The banking industry witnessed significant expansion in the loan book. 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 2018 (11.9%). This will create a challenge for some of the players.

Relative Position BAFL is ranked amongst top 5 banks on the basis of its strong growth trajectory in advances and profitability. BAFL’s customer deposits (Sep18: PKR 649 bln) increased by ~5% inline with the sector’s growth of 6%. Bank’s share in total deposits of the sector remained at 5.2%.

Revenues Total net revenue for the nine months improved 5% YoY and stands at PKR 31.4 Bln. The growth in Net Interest Income was primarily due to improved volumes and spreads, despite maturity of high yielding PIBs. The predominant elements in non-markup income are higher foreign exchange, core fee and commission earnings which are offset by lower capital gains being a market phenomenon.

Performance ROE of the Bank increased 60bps from 18.1% in Sep17 to 18.7% in Sep18 owing to surge in markup and non-markup income. Further, during nine months period an overall specific provision net reversal of PKR 603 mln was recorded (Dec17: PKR 510 mln).

Sustainability Going forward, fresh perspectives, innovative ideas and renewed commitment should be given importance. BAFL is successfully working towards achieving its ambition of becoming a truly digital bank and an innovative financial institution in Pakistan.

Financial Risk

Credit Risk Advances book continued to remain concentrated in Corporate (Sep18: 48% Dec17: 48%) and Commercial (Sep18: 26% Dec17: 29%) borrowers. Recoveries against non-performing advances continued to outpace fresh charge booked against delinquent loans, as NPLs decreased from PKR 17.6 bln at Dec17 to PKR 17 bln at Sep18. Bank’s coverage ratio stands at 93%, while the Bank’s NPL ratio stands at 3.5%, and remains one of the lowest in the industry.

Market Risk Market risk, in terms of BAFL’s exposure of investment book, is now representing 26% of total earning assets as at Sep18 witnessed a dip from 45% at Dec17, owing to shrinkage of investment book due to maturity of government securities. Investments continued to remain concentrated in government securities (Sep18: 94%; Dec17: 97%).

Liquidity And Funding Subordinated loan (TFC V Unsecured) with an issue size of PKR 5 bln was issued in Feb13. 0.30% of the principal will be redeemed in the first 90 months and remaining principal of 99.70% at maturity in the 96th month. Profit rate will be six months KIBOR plus 1.25%. Total customer deposits grew by mere 4.9% to PKR 649 bln which is inline industry growth of 6.2%. Further, the Bank is focusing more on low/ no cost deposits, high cost deposits were shed to reduce the cost of deposits. The portion of CASA stood at 76.5% (Dec17: 78.8%). Advances-to-deposits ratio increased to 69.5% at Sep18 (Dec17: 61.3%).

Capitalization Bank remains adequately capitalized, with CAR for Sep18, reported at 15% (Dec17: 13.7%). Out of total issue size of BAFL’s TFC V (PKR 5 bln), PKR 11 mln has been repaid in 11 equal semi-annual installments. Next payment will be due in Feb, 2019. During the period, the Bank issued fully paid up, rated, listed, perpetual, unsecured, subordinated, non-cumulative and contingent convertible debt instruments in the nature of TFCs, which qualify as Additional Tier I, with an issue size of PKR 7 bln.



Bank Alfalah Limited

BALANCE SHEET	30-Sep-18	31-Dec-17	31-Dec-16	31-Dec-15
Earning Assets				
Advances-Performing	471,618	399,603	376,845	331,896
Debt Instruments	13,057	14,260	12,505	10,826
Total Finances	484,674	413,863	389,350	342,722
Investments	199,046	386,553	376,683	412,329
Others	86,456	60,439	45,867	51,443
	770,176	860,854	811,900	806,494
Non Earning Assets				
Non-Earning Cash	66,236	63,348	67,726	55,104
Deferred Tax	-	-	-	-
Net Non-Performing Finances	892	973	1,781	2,207
Fixed Assets & Others	57,066	63,654	36,051	38,802
	124,194	127,975	105,558	96,113
TOTAL ASSETS	894,371	988,829	917,457	902,608
Funding				
Deposits	680,497	653,406	640,944	640,189
Borrowings	88,683	211,215	186,629	182,376
	769,179	864,621	827,573	822,565
Non Interest Bearing Liabilities	55,606	58,408	29,759	26,689
TOTAL LIABILITIES	824,785	923,029	857,332	849,254
EQUITY (including revaluation surplus)	69,585	65,800	60,125	53,353
Total Liabilities & Equity	894,371	988,829	917,457	902,608
INCOME STATEMENT	30-Sep-18	31-Dec-17	31-Dec-16	31-Dec-15
Interest / Mark up Earned	42,904	56,919	57,245	61,458
Interest / Mark up Expensed	(19,662)	(27,639)	(28,474)	(32,811)
Net Interest / Markup revenue	23,242	29,281	28,770	28,648
Other Income	8,159	9,894	8,868	8,841
Total Revenue	31,401	39,175	37,638	37,489
Non-Interest / Non-Mark up Expensed	(17,763)	(25,389)	(23,432)	(22,598)
Pre-provision operating profit	13,638	13,785	14,206	14,891
Provisions	623	260	(1,183)	(2,287)
Pre-tax profit	14,261	14,045	13,023	12,604
Taxes	(5,632)	(5,678)	(5,123)	(5,081)
Net Income	8,629	8,367	7,900	7,523
Ratio Analysis	30-Sep-18	31-Dec-17	31-Dec-16	31-Dec-15
Performance				
ROE	19% *	16%	17%	19%
Cost-to-Total Net Revenue	57%	65%	62%	60%
Provision Expense / Pre Provision Profit	-5%	-2%	8%	15%
Capital Adequacy				
Equity/Total Assets	7%	6%	5%	5%
Capital Adequacy Ratio as per SBP	15%	14%	13%	13%
Funding & Liquidity				
Liquid Assets / Deposits and Borrowings	41%	47%	47%	52%
Advances / Deposits	69%	61%	59%	52%
CASA deposits / Total Customer Deposits	79%	79%	85%	77%
Intermediation Efficiency				
Asset Yield	7% *	7%	7%	9%
Cost of Funds	3% *	3%	4%	5%
Spread	4% *	3%	4%	4%
Outreach				
Branches	640	637	639	653



Regulatory and Supplementary Disclosure

Nature of Instrument	Size of Issue (PKR)	Tenor	Security	Quantum of Security	Nature of Assets	Trustee	Book Value of Assets
Term Finance Certificate (TFC)	5,000 mln	8 years	Unsecured (subordinated as to the payments of principal and profit to all other indebtedness of BAFL)	N/A	N/A	Pak Brunei Investment Company	N/A

Bank Alfalah Limited TFC Feb' 13	
Name of Issuer	Bank Alfalah Limited
Issue size	PKR 5,000 mln
Issue Date	20-Feb-13
Tenor	8 years
Maturity	20-Feb-21
Profit Rate	6 MK + 1.25%
Principal Repayment	0.30% of the principal will be redeemed in the first 90 months and remaining principal of 99.70% at maturity in the 96th month.
Security	Unsecured (subordinated as to the payments of principal and profit to all other indebtedness of BAFL)

Bank Alfalah Limited TFC Feb' 13 Redemption Schedule								
Due Date Principle	Opening Principal	Principal Repayment	Due Date Markup/ Profit	Markup/ Profit Rate	6M Kibor	Markup/Profit Payment	Installment Payable	Principal Outstanding
	PKR in mln					PKR in mln		
20-Feb-13	5,000	-						5,000
20-Aug-13	5,000	1	20-Aug-13	6 MK + 1.25%	9.44%	265	266	4,999
20-Feb-14	4,999	1	20-Feb-14	6 MK + 1.25%	9.11%	261	262	4,998
20-Aug-14	4,998	1	20-Aug-14	6 MK + 1.25%	10.16%	283	284	4,997
20-Feb-15	4,997	1	20-Feb-15	6 MK + 1.25%	10.18%	288	289	4,996
20-Aug-15	4,996	1	20-Aug-15	6 MK + 1.25%	8.47%	241	242	4,995
20-Feb-16	4,995	1	20-Feb-16	6 MK + 1.25%	7.06%	209	210	4,994
20-Aug-16	4,994	1	20-Aug-16	6 MK + 1.25%	6.35%	190	191	4,993
20-Feb-17	4,993	1	20-Feb-17	6 MK + 1.25%	6.01%	183	184	4,992
20-Aug-17	4,992	1	20-Aug-17	6 MK + 1.25%	6.14%	183	184	4,991
20-Feb-18	4,991	1	20-Feb-18	6 MK + 1.25%	6.15%	186	187	4,990
20-Aug-18	4,990	1	20-Aug-18	6 MK + 1.25%	6.43%	190	191	4,989
20-Feb-19	4,989	1	20-Feb-19	6 MK + 1.25%	8.05%	231	232	4,988
20-Aug-19	4,988	1	20-Aug-19	6 MK + 1.25%	8.05%	228	229	4,987
20-Feb-20	4,987	1	20-Feb-20	6 MK + 1.25%	8.05%	231	232	4,986
20-Aug-20	4,986	1	20-Aug-20	6 MK + 1.25%	8.05%	229	230	4,985
20-Feb-21	4,985	4,985	20-Feb-21	6 MK + 1.25%	8.05%	231	5,216	-
		5,000				3,629	8,629	

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.		
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+:	The highest 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.	A1:	A strong capacity for timely repayment.
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.	A2:	A satisfactory capacity for timely repayment. This may be 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.	A3:	An adequate capacity for timely repayment. Such capacity is 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.	B:	The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions.
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.	C:	An inadequate capacity to ensure timely repayment.
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) 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	

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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

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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.
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- (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)
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- (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)
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- (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)

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- (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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