The Pakistan Credit Rating Agency Limited

Rating Report

Bank Alfalah Limited | TFC V | Feb-13

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
28-Dec-2019	AA	-	Stable	Maintain	-
28-Jun-2019	AA	-	Stable	Maintain	-
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	-
30-Jun-2015	AA-	-	Positive	Maintain	-
30-Jun-2014	AA-	-	Stable	Maintain	-
28-Jun-2013	AA-	-	Stable	Maintain	-
14-Nov-2012	AA-	-	Stable	Initial	-

Rating Rationale and Key Rating Drivers

The rating reflects the bank's sustained performance, good asset quality, strong financial profile and healthy liquidity. The bank has solidified its relative positioning in the universe of large sized banks by improving its market share. The bank's advances maintained at a healthy level, resulting in a good ADR of ~67%, which is on the higher end among large banks. The mix of deposits improved as the bank added a few percentage points to the CA part in the CASA mix. Resultantly, BAFL's cost of funds is comparable to some of the large banks. The Bank has a sound foothold with a considerable presence across the country which has enabled its deposit base to sustain. Operating cost structure has improved on YoY basis on account of cost rationalization. The Bank saw healthy maintenance in its profitability. Overall infection ratio remained stable. Effective implementation of the envisaged business strategy has played an important role in business growth. The increasing asset yield and cost efficiency enabled spreads to increase. Investment yield has a notable improvement.
The rating draws comfort from the bank's experienced management team, prudent risk management policies and deep rooted relationship with clients - borrowers as well as depositors. The bank issued Tier-I instrument, augmenting the bank's CAR and providing room for growth.

The rating is dependent on the bank's sustained risk profile. The equity base of the bank and CAR are satisfactory and may continually be enhanced in view of the expected growth in loans. Augmentation of the Bank's capitalization backed by strong sponsors and adding granularity to its advances and deposits book are essential. The effective management of spreads remains important, meanwhile, holding the asset quality is a pre-requisite.

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	PACRA_Methodology_FI(Jun-19),PACRA_Methodology_DI Basel III_FY19(Jun-19),Criteria | Rating Modifier(Jun-19)
Related Research	Sector Study | Commercial Bank(Jun-19)
Rating Analysts	Usama Liaquat | usama.liaquat@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 648 branches spanning in more than 200 cities in Pakistan.

Operations In collaboration with International Finance Corporation (IFC) - a member of the World Bank Group - the bank altered its model from only offering credit services to providing a complete range of banking services to SME customers.

Ownership

Ownership Structure BAFL is majority owned by the Abu Dhabi Group (ADG) (49.19%), rest is owned by IFC (14.74%), Mutual funds, other NBFIs (27.61%) and General public (8.46%).

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.

Financial Strength Sponsors, being ruling family of UAE, possess strong financial ability to support BAFL in case of need.

Governance

Board Structure 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 Mabarak Al Nahayan, is a prominent member of the ruling family of Abu Dhabi, UAE. He owns substantial business interests, hotels and other investments in the UAE, Pakistan, Africa, USA and Central Asia.

Board Effectiveness The board actively participates in strategy formulation and effectively monitors the managerial affairs of the bank. To ensure effective and independent oversight of the bank’s overall operations, the Bank has constituted six committees.

Financial Transparency The external auditors of the Bank, EY Ford Rhodes, Chartered Accountants, issued an unqualified audit opinion pertaining to annual financial statements for 2018.

Management

Organizational Structure BAFL has a lean organizational structure that clearly defines responsibilities, authority and reporting lines with proper monitoring and compliance mechanism.

Management Team Bank’s senior management team comprises experienced bankers having national and international exposure. Mr. Nauman Ansari, CEO, joined Bank Alfalah as President and CEO in July 2017 and has served various banks during his 26-year professional career,including leading institutions like SCB, Bank of America, ABN AMRO, Fortis Bank, Faysal bank and Samba.

Effectiveness Bank Alfalah has three main management committees for the purpose of strategic planning and decision-making under the Chairmanship of the CEO.

MIS The bank uses Temenos (T-24) as its core banking software across all branches. The Bank’s core banking system is well recognized for its high stability and efficiency; a result of carefully planned performance-enhancements, architectural redesigning, optimization along with a large number of successfully in-house developed T24 new products.

Risk Management Framework The Board Risk Management Committee (BRMC) is appointed and authorized by the Board of Directors (BOD) to assist in design, regular evaluation and timely updating of the risk management framework of the Bank.

Business Risk

Industry Dynamics Despite challenging macroeconomic environment, banking sector maintained its growth trajectory during 9MCY19, backed by decent growth in deposits (9MCY19: PKR 14,945bln; 9MCY18: 13,603bln). However, deployment was largely skewed towards investments and particularly towards government instruments due to favourable interest rate dynamics (9MCY19: PKR 9,641bln; 9MCY18: 6,942bln). Meanwhile, advances witnessed a slowdown owing to subdued economic activity, cautious lending approach and monetary tightening (9MCY19: PKR 8,014bln; 9MCY18: 7,422bln). Asset quality saw some deterioration – increased NPLs, particularly in sugar and energy sectors (9MCY19: PKR 758 bln, 9MCY18: 637bln). The profitability of the banking sector improved due to increase in Net Interest Income, which translated positively in other profitability indicators. The overall risk profile of the banking sector remained satisfactory.

Relative Position BAFL is ranked among the large banks of the country, on the basis of its strong growth trajectory in net advances and profitability. During 9MCY19, Bank’s customer deposits (PKR 678 bln) increased by ~3.7%. BAFL retained a good position in the banking sector with share in customer deposits of the sector at 4.8% (Dec18: 4.6%).

Revenues On the revenue front, net markup income and non-markup income showed combined growth of 29% YoY. Non-markup income was reported at PKR 7bln, a decrease of 11.2% over corresponding period last year, led by growth in foreign exchange income & fee, despite capital loss on securities due to bearish capital market.

Performance The Bank recorded a growth of 7% YTD in profit after tax with a challenging operating environment. The Bank’s PBT for the year stands at PKR 16.49bln as against PKR 14.26bln last Sep, showing improvement of 15.6%. PAT of PKR 9.24bln as against PKR 8.62bln 9MCY18, saw improvement of 7%. The significant growth in net revenue was not effectively translated in the PAT due to additional Super Tax charge levied through the mini budget, higher provisioning and capital loss.

Sustainability Looking ahead, Bank Alfalah is well-positioned for strong growth and building long-term shareholder value. The Bank will continue to focus on building a low-cost deposit base, improving the return on capital on risk assets, optimizing returns from the banking book and enforcing a strong cost discipline across the Bank.

Financial Risk

Credit Risk As of Sept 2019 net advances of the Bank were reported at PKR 473 bln constituting around 45% of the Bank’s total assets; largely remaining at same level on YoY basis as compared to net advances of PKR 501Bln and PKR 400Bln for CY18 & CY17 respectively. The Non-performing loan base of the Bank witnessed an increase of PKR 1.8 bln, on the basis of subjective classification and prudence, and was reported at PKR 20.7 bln. Additionally, the NPL ratio was recorded at 4.2% as compared to CY18 ratio of 3.6%; yet continuing to remain one of the lowest infection ratios in the industry.

Market Risk Following the significant investment in PIBs, the investment portfolio depicted an increase of 26%, amounting to PKR 350 bln during 9MCY19 (CY18: PKR 277 bln). The government securities continue to dominate the overall investment book. Net investments for the period have increased by PKR 72 bln with a corresponding increase in Lending to Financial Institutions by PKR 14 bln to capitalize on evaluating the opportunities.

Liquidity And Funding Bank’s focus throughout the year remained on improving deposit profile and managing spreads, Total Deposits were reported at PKR 711 bln as of Sep-19 against PKR 703 bln in Dec-18; growth is mainly driven by 11.6% surge in current accounts. ADR ratio stood at 67% in Sept-19, as compared to 71% in Dec 2018.

Capitalization Bank’s CAR as on Sep-19 stands at 16.87% (Dec-18: 14.95%, Dec17: 13.39%), which is well-above the regulatory requirement of 11.90%; the increase in CAR level from Dec-18 to Sept-19 is mainly due to reduction in credit risk RWAs and increase in Eligible Capital Base. Higher Quality of capital is evident from Bank’s Common Equity Tier-I (CET-I) to Total Risk Weighted Assets (RWA) ratio, which comes to 12.06% against the regulatory requirement of 6.00%.

PKR mln

Bank Al Falah Listed Public Limited	Sep-19 9M	Dec-18 12M	Dec-17 12M	Dec-16 12M
A BALANCE SHEET				
1 Total Finances - net	477,715	508,254	408,224	378,113
2 Investments	342,312	268,977	392,112	387,825
3 Other Earning Assets	91,051	75,107	59,786	45,867
4 Non-Earning Assets	134,540	151,814	137,653	103,777
5 Non-Performing Finances-net	3,114	2,066	1,052	1,876
Total Assets	1,048,732	1,006,218	998,828	917,457
6 Deposits	711,262	702,895	644,985	640,944
7 Borrowings	185,095	135,727	212,185	186,629
8 Other Liabilities (Non-Interest Bearing)	69,709	91,948	75,859	29,759
Total Liabilities	966,065	930,571	933,028	857,332
Equity	82,667	75,647	65,800	60,125
B INCOME STATEMENT				
1 Mark Up Earned	66,435	59,318	56,176	57,144
2 Mark Up Expensed	(33,124)	(27,727)	(27,199)	(28,153)
3 Non Mark Up Income	7,106	10,675	9,277	8,907
Total Income	40,417	42,266	38,253	37,899
4 Non-Mark Up Expenses	(21,908)	(24,365)	(24,964)	(23,802)
5 Provisions/Write offs/Reversals	(2,012)	(588)	616	(1,073)
Pre-Tax Profit	16,496	17,313	13,906	13,023
6 Taxes	(7,254)	(6,687)	(5,539)	(5,123)
Profit After Tax	9,242	10,625	8,367	7,900
C RATIO ANALYSIS				
1 Performance				
Net Mark Up Income / Avg. Assets	4.3%	3.2%	3.0%	3.2%
Non-Mark Up Expenses / Total Income	54.2%	57.6%	65.3%	62.8%
ROE	15.6%	15.0%	13.3%	13.9%
2 Capital Adequacy				
Equity / Total Assets (D+E+F)	7.9%	7.5%	6.6%	6.6%
Capital Adequacy Ratio	16.9%	15.0%	13.8%	13.2%
3 Funding & Liquidity				
Liquid Assets / (Deposits + Borrowings Net of Repo)	39.7%	38.5%	42.5%	46.8%
(Advances + Net Non-Performing Advances) / Deposits	66.5%	71.4%	62.1%	59.1%
CA Deposits / Deposits	45.1%	40.9%	46.0%	56.0%
SA Deposits / Deposits	33.7%	34.5%	32.9%	31.1%
4 Credit Risk				
Non-Performing Advances / Gross Advances	4.2%	3.6%	4.2%	4.8%
Non-Performing Finances-net / Equity	3.8%	2.7%	1.6%	3.1%

Debt Instrument Rating Scale & Definitions

Credit rating reflects forward-looking opinion on credit worthiness of underlying 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

Rating	Definition
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

Rating	Definition
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.

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

Regulatory and Supplementary Disclosure

(Credit Rating Companies Regulations,2016)

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)

Proprietary Information

Regulatory and Supplementary Disclosure

Bank Alfalah Limited | TFC V | Feb-13

Nature of Instrument	Size of issue	Date of Issue	Years	Security	Quantum of security	Nature of Assets	Book value of Assets (PKR mln) March 2019	Trustee
TFC	5,000 mln	20/02/2013	8 years (unless Call Option is exercised)	Unsecured (subordinated as to the payments of principal and profit to all other indebtedness of BAFL)	N/A	N/A	N/A	Pak Brunei Investment Company

Liberty Power Tech Limited |TFF| Jan-11 | Redemption Schedule

Due Date Principle*	Opening Principal	Principal Repayment*	Due Date Markup/ Profit*	6M Kibor + 1.25% (fixed)	6M Kibor	Markup/Profit Payment	Installment Payable	Principal Outstanding
	PKR in mln					PKR in mln		
Issuance								5,000
6 months from issuance	5,000	1	6 months from issuance	10.69%	4.99%	265	266	4,999
12 months from issuance	4,999	1	12 months from issuance	10.36%	9.67%	261	262	4,998
18 months from issuance	4,998	1	18 months from issuance	11.41%	10.13%	283	284	4,997
24 months from issuance	4,997	1	24 months from issuance	11.43%	9.86%	288	289	4,996
30 months from issuance	4,996	1	30 months from issuance	9.72%	7.58%	241	242	4,995
36 months from issuance	4,995	1	36 months from issuance	8.31%	6.64%	209	210	4,994
42 months from issuance	4,994	1	42 months from issuance	7.61%	6.26%	190	191	4,993
48 months from issuance	4,993	1	48 months from issuance	7.28%	6.08%	183	184	4,992
54 months from issuance	4,992	1	54 months from issuance	7.38%	6.14%	183	184	4,991
60 months from issuance	4,991	1	60 months from issuance	7.40%	6.18%	186	187	4,990
66 months from issuance	4,990	1	66 months from issuance	7.68%	6.79%	190	191	4,989
72 months from issuance	4,989	1	72 months from issuance	9.30%	9.57%	234	235	4,988
78 months from issuance	4,988	1	78 months from issuance	12.09%	11.93%	299	300	4,987
84 months from issuance	4,987	1	84 months from issuance	15.33%	13.73%			4,986
90 months from issuance	4,986	1	90 months from issuance	14.98%	13.73%			4,985
96 months from issuance	4,985	4,985	96 months from issuance	14.98%	13.73%			0
		5,000				**3012**	**3025**	