



The Pakistan Credit Rating Agency Limited

# BANK ISLAMI PAKISTAN LIMITED

	<b>NEW [OCT-16]</b>	<b>PREVIOUS [MAY-16]</b>
Long-Term	A+	A+
Short-Term	A1	A1
Action	Maintain	Rating Watch
Outlook	Rating Watch Developing	Developing

## REPORT CONTENTS

1. RATING ANALYSES
2. FINANCIAL INFORMATION
3. RATING SCALE
4. REGULATORY AND SUPPLEMENTARY DISCLOSURE

OCTOBER 2016

**Profile & Ownership**

- BankIslami Pakistan Limited (BIPL), established in 2004, is the first Islamic bank receiving Islamic Banking license to operate in the country.
- BIPL is listed on Pakistan Stock exchange; the bank offers a wide range of Shariah compliant products and services.
- The bank operates through a network of 317 branches as at end-Mar16.
- Post right issue in May 2015, major shareholders of the bank is JSCL (21%), Mr. Ali Hussain and SAJ Capital (~21%), Randeree Family (~20%) and Dubai Bank (14%).
- In May 2015, BIPL acquired defunct KASB Bank Limited.

**Governance**

- Currently the board comprises eight-members including the CEO.
- Two board members represent JSCL, two Randerees, one Dubai bank and one SAJ Capital, whereas currently one position of the board is vacant.
- The board comprises qualified and experienced professionals.
- Mr. Ali Hussain, MD SAJ Capital Limited, is the Chairman of the Board.
- BIPL's shariah board comprises three leading Islamic scholars of the country, namely (i) Mufti Irshad Ahmad Aijaz, ii) Mufti Muhammad Hussain, and iii) Mufti Javed Ahmad.
- During the acquisition process of defunct KASB Bank Limited, the shariah board has played an instrumental role in facilitating the conversion of conventional banking assets into Islamic assets.
- Owing to ongoing fair valuation process of KASB's assets, the bank had faced delay in finalizing the quarterly and annual accounts.

**Management**

- Mr. Hassan A Bilgrami, the President of the bank has been instrumental in the growth of the bank. He has been associated with the bank since its inception.
- To date, BIPL has settled all operational and HR related matters post-acquisition.

**Risk Management**

- Given acquisition of KASB bank, the bank's net advances, 39% of the total assets at end CY15 (CY14: 39%), witnessed 65% YoY growth.
- Owing to addition of significant non performing book of KASB, non-performing advances increased, in turn, NPL ratio rose (1HCY16: 14.6%; CY15: 18.5%; CY14: 2.5%); however, majority (91%) of these loans are provided.
- Advances' concentration in terms of top-20 increased to 52% (CY15: 58%; CY14: 18%).

**Performance**

- During CY15, the bank posted a decline in its spreads, owing to increased cost of deposits.
- Support from other income and reversal in provisioning provided respite to the bank's bottom-line (1HCY16: PKR 359mln; CY15: PKR -196mln; CY14: PKR 314mln); however pre-provision performance is likely to remain under pressure, particularly in comparison to peers.
- Post-merger operational issues are largely settled. Going forward, the bank aims to considerably expand its lending portfolio funded through low cost deposits. Recovery from non-performing loans of defunct bank is also a priority.
- Concentration in top 20 deposits improved (CY15: 30%, CY14: 39%); although to manage earnings retention of bank's top deposit is critical at least in the medium term.

**Capital and Funding**

- The bank would maintain focus on low cost deposits. The share of CASA in the total deposits stood at 71% at end 1HCY16 (CY15: 67%; CY14: 61%), which bodes well for cost rationalization.
- The bank's liquidity position evident by Liquid assets to Deposits & Borrowing ratio (1HCY16: 46%; CY15: 27%; CY14: 40%) is improving.
- Post equity injection, BIPL is MCR compliant with a CAR of 12.95% at end 1HCY16.

**RATING RATIONALE**

The ratings reflect BankIslami's established position in the country's Islamic banking space. With the acquisition of erstwhile KASB Bank in May 2015, BankIslami's system share in deposits improved. Post-acquisition, BIPL had faced significant withdrawal of deposits, owing to removal of moratorium imposed on erstwhile KASB Bank. However, same was managed successfully. Moreover, this acquisition resulted in i) increase in footprint, ii) deposit base, and iii) strategic investment book. The Bank also inherited carried forward tax losses and a sizeable portfolio of non-performing assets; that has its own challenges and opportunities. To compensate the Bank for negative net worth of the defunct KASB Bank, it was also provided low cost subordinated loan facility from SBP; supporting Bank's revenue and CAR. Although BankIslami has enhanced deposit base, yet risk of withdrawal from key depositor acquired through amalgamation (representing 13% in total deposit) remains. Given time required to fully absorb KASB Bank related costs, operational performance is under pressure. Meanwhile, recoveries from non-performing loans provide support and lately BIPL has started progressing to achieve profitability. The management, while synergizing on enhanced outreach intends to pursue growth.

**KEY RATING DRIVERS**

The ratings require sustainable improvement in operational performance, in turn, maintaining positive trend in bottom-line. At the same time maintaining a strong capital adequacy while pursuing growth is important. Any downward spiral in profits, or incidence of non-performing assets may negatively impact the ratings. Meanwhile, ratings remain on Watch to monitor ascend forward profitability from core operations and manage any unforeseen issues related to erstwhile KASB Bank.



PKR mln

BALANCE SHEET	30-Sep-16 9MCY16	31-Dec-15 Annual	31-Dec-14 Annual	31-Dec-13 Annual
<b>Earning Assets</b>				
Advances	79,617	67,215	40,636	37,823
Debt Instruments	2,209	1,100	1,331	1,244
Total Finances	81,826	68,315	41,968	39,067
Investments	69,962	34,786	29,053	30,090
Others	12,546	41,605	18,877	7,472
	<b>164,334</b>	<b>144,706</b>	<b>89,898</b>	<b>76,630</b>
<b>Non Earning Assets</b>				
Non-Earning Cash	7,524	9,036	6,361	4,890
Deferred Tax	6,009	6,591	-	-
Net Non-Performing Finances	1,819	1,579	731	762
Fixed Assets & Others	13,131	12,319	4,994	4,574
	<b>28,483</b>	<b>29,525</b>	<b>12,086</b>	<b>10,226</b>
<b>TOTAL ASSETS</b>	<b>192,816</b>	<b>174,231</b>	<b>101,984</b>	<b>86,856</b>
<b>Interest Bearing Liabilities</b>				
Deposits	155,074	153,058	90,331	75,226
Borrowings	18,254	3,198	561	2,538
	173,328	156,256	90,892	77,764
<b>Non Interest Bearing Liabilities</b>	7,213	6,789	4,225	2,850
<b>TOTAL LIABILITIES</b>	<b>180,541</b>	<b>163,044</b>	<b>95,117</b>	<b>80,613</b>
<b>EQUITY (including revaluation surplus)</b>	<b>12,275</b>	<b>11,186</b>	<b>6,867</b>	<b>6,242</b>
<b>TOTAL LIABILITIES &amp; EQUITY</b>	<b>192,816</b>	<b>174,231</b>	<b>101,984</b>	<b>86,856</b>

INCOME STATEMENT	30-Sep-16 9MCY16	31-Dec-15 Annual	31-Dec-14 Annual	31-Dec-13 Annual
Profit / Return Earned	7,624	8,834	7,812	6,289
Return Expensed	(4,375)	(5,119)	(4,459)	(3,790)
<b>Net Revenue</b>	<b>3,249</b>	<b>3,715</b>	<b>3,353</b>	<b>2,500</b>
Other Income	517	570	632	454
<b>Total Revenue</b>	<b>3,765</b>	<b>4,285</b>	<b>3,985</b>	<b>2,953</b>
Other Expenses	(4,457)	(5,188)	(3,498)	(2,522)
Pre-provision operating profit	(692)	(903)	487	431
Provisions	1,698	631	(17)	(123)
Pre-tax profit	1,006	(272)	470	308
Taxes	(412)	76	(156)	(123)
<b>Net Income</b>	<b>595</b>	<b>(196)</b>	<b>314</b>	<b>185</b>

RATIO ANALYSIS	30-Sep-16 9MCY16	31-Dec-15 Annual	31-Dec-14 Annual	31-Dec-13 Annual
<b>Performance</b>				
ROE	22.0%	-2.4%	5.3%	3.4%
Cost-to-Total Net Revenue	121.3%	122.9%	88.7%	87.7%
Provision Expense / Pre Provision Profit	245.5%	69.8%	3.6%	28.5%
<b>Capital Adequacy</b>				
Equity/Total Assets	5.7%	5.9%	6.1%	6.3%
Capital Adequacy Ratio as per SBP	13.0%	12.3%	17.0%	15.7%
<b>Funding &amp; Liquidity</b>				
Liquid Assets / Deposits and Borrowings	44.5%	27.1%	39.6%	46.0%
Advances / Deposits	52.5%	44.9%	45.5%	50.9%
CASA deposits / Total Customer Deposits	68.9%	67.1%	60.6%	53.4%
<b>Intermediation Efficiency</b>				
Asset Yield	19.1%	7.6%	9.4%	8.9%
Cost of Funds	10.3%	4.1%	5.3%	5.3%
Spread	8.8%	3.4%	4.1%	3.6%
<b>Outreach</b>				
Branches	317	317	213	201



## STANDARD RATING SCALES & 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.

<b>LONG TERM RATINGS</b>		<b>SHORT TERM RATINGS</b>
<b>AAA</b>	<p><b>Highest credit quality.</b> Lowest expectation of credit risk.</p> <p>Indicate exceptionally strong capacity for timely payment of financial commitments.</p>	<p><b>A1+:</b> The highest capacity for timely repayment.</p> <p><b>A1:</b> A strong capacity for timely repayment.</p> <p><b>A2:</b> A satisfactory capacity for timely repayment. This may be susceptible to adverse changes in business, economic, or financial conditions.</p> <p><b>A3:</b> An adequate capacity for timely repayment. Such capacity is susceptible to adverse changes in business, economic, or financial conditions.</p> <p><b>B:</b> The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions.</p> <p><b>C:</b> An inadequate capacity to ensure timely repayment.</p>
<b>AA+</b> <b>AA</b> <b>AA-</b>	<p><b>Very high credit quality.</b> Very low expectation of credit risk.</p> <p>Indicate very strong capacity for timely payment of financial commitments. This capacity is not significantly vulnerable to foreseeable events.</p>	
<b>A+</b> <b>A</b> <b>A-</b>	<p><b>High credit quality.</b> Low expectation of credit risk.</p> <p>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.</p>	
<b>BBB+</b> <b>BBB</b> <b>BBB-</b>	<p><b>Good credit quality.</b> Currently a low expectation of credit risk.</p> <p>The capacity for timely payment of financial commitments is considered adequate, but adverse changes in circumstances or economic conditions are more likely to impair this capacity.</p>	
<b>BB+</b> <b>BB</b> <b>BB-</b>	<p><b>Moderate risk.</b> Possibility of credit risk developing.</p> <p>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.</p>	
<b>B+</b> <b>B</b> <b>B-</b>	<p><b>High credit risk.</b></p> <p>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.</p>	
<b>CCC</b> <b>CC</b> <b>C</b>	<p><b>Very high credit risk.</b></p> <p>“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.</p>	
<b>D</b>	Obligations are currently in default.	

### 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. Rating Watch may carry designation – Positive (rating may be raised, negative (lowered), or developing (direction is unclear). A watch should be resolved within foreseeable future, but may continue if underlying circumstances are not settled.

### 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’.

### 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, a suspended 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, or e) the entity/issuer defaults.

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[Name of Rated Entity](#)  
[Sector](#)  
[Type of Relationship](#)

BankIslami Pakistan Limited  
 Banking  
 Solicited

[Purpose of the Rating](#)

Regulatory Requirement  
 Independent Risk Assessment

[Rating History](#)

Dissemination Date	Long Term	Short Term	Outlook	Action
6-May-16	A+	A1	Developing	Rating Watch
08-May-15	A+	A1	Rating Watch	Maintain
17-Apr-15	A+	A1	Stable	Upgrade
30-Jun-14	A	A1	Positive	Maintain
15-Jul-13	A	A1	Positive	Maintain
29-Jun-12	A	A1	Stable	Maintain

[Applicable Criteria and Related Research](#)

Banking Rating Methodology  
 Islamic Banking - View Point | Feb -16

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[Rating Team Statement](#)

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PACRA initiates immediate review of the outstanding rating(s) upon becoming aware of any information that may be reasonable be expected to result in any change (including downgrade) in the rating

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 PACRA has framed and implemented whistle-blower policy encouraging all employees to intimate the compliance officer any unethical practice or misconduct relating to the

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[Probability of Default \(PD\)](#)

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