The Pakistan Credit Rating Agency Limited

SONERI BANK LIMITED

TFCs Issue (Unsecured, Subordinated)	New [Dec-16]	Previous [Jun-16]
TFCs (*PKR 3,000mln*)	A+	A+

REPORT CONTENTS

DECEMBER 2016

Profile & Ownership

- Soneri Bank Limited (SBL), incorporated in Sep91, is a small size commercial bank having 1.8% deposit share in the system at end-Sep16
- Operating with a network of 281 branches and 295 ATMs across the country
- Feerasta Family – sponsors of Rupali Group – holds controlling stake (~58%), followed by NIT (~11%), while rest is spread across general public and others

Governance & Management

- Eight member board including the President. Out of remaining two directors represent Feerasta Family, two are NIT nominees, while three are independent members
- Experienced management team; operations divided into thirteen functions
- The President and CEO, Mr. Aftab Manzoor, carries over three decades of international banking experience; supported by COO, Mr. Amin A. Feerasta

Risk Management

- Migration of Temonos (T24) – core banking system – expected to start by Jul17
- During 9MCY16, earnings assets increased by ~5% mainly driven by rise in investment book. Lending portfolio declined by 11% to PKR 96bln. Sectoral concentration remained high (top 3 sectors comprising more than half of advances) 9MCY16: 53% (CY15: 59%), with textile at top (22%); Top-20 private performing clients' concentration inched down (9MCY16: 26%, 9MCY15: 29%) – on account of cautious lending
- The bank's advances to deposit ratio dropped to ~49% at 9MCY16 (9MCY15 57%) – at par with industry
- During 9MCY16, asset quality largely maintained; infection ratio – NPLs to gross advances (end-Sep16: 10%) remained same – mainly due to decrease in NPLs and advances. Nevertheless, due to nominal provisioning (due to reversals), the banks' loan loss coverage ratio improved (end-Sep16: 78%, end-Dec15: 74%)
- At end-Sep16, investment portfolio, comprising 52% of earning assets, (witnessed ~14% growth); dominated by government securities (98%) – mix (T-Bills: 43%, PIBs: 55%) change in favor of T-Bills

Business Risk

- In line with industry, performance remained subdued; NIMR registered 6% YoY decrease despite volumetric increase in earning assets. Asset yield decreased YoY – at par with industry – on account of lower benchmark rates. Cost of funds declined but wasn't significant to secure spread. Hence Spread reduced to 3.1% (9MCY15: 3.9%)
- Non-markup income stood at PKR 2.1bln (9% decrease). During 9MCY16, cost to total net revenue increased to 65% (CY15: 57%) primarily due to addition of new branches
- During 9MCY16, the bank posted net profit (PKR 1.5bln; down 3%)

Capital & Funding

- Deposits increased by ~9% YoY with an addition of PKR 16bln; CASA slightly improved (end-Sep16: ~72%, end-Dec15: 69%)
- Top-20 depositors' concentration significantly increased to 25% (CY15: 19%), due to increase in ticket size
- Overall liquidity position strengthened due to continuous rise in liquid investments**;** Capitalization remained healthy with CAR standing at 15.4% at end-Sep16

TFC Issue

- SBL issued 2nd subordinated, unsecured, and listed TFC of PKR 3,000mln in Jul15 having a tenor of eight years. Profit rate is 6MK plus 135bps p.a. payable semi-annually in arrears. Principal repayment (99.7%) would be in bullet form at maturity (2023). SBL retains call option; exercisable in Jul20
- The issue carries a lock-in clause that stops payment if SBL falls below MCR. The instrument is also subject to loss absorbency
- Cushion to loss absorbency ranges from ~3% to ~5%, incorporating the projections

RATING RATIONALE

The rating reflects SBL's maintained business profile as the bank managed to hold its system share in deposits (1.8%). Despite YoY volumetric rise in earning assets, mainly on account of surge in investment portfolio, the spreads came under pressure – a phenomenon witnessed industry-wide on the back of lower prevailing interest rates. The management strives to reduce costs of funds through mobilization of current deposits; material progress remains to be seen. The management's strategy incorporates increase in advances; however, the bank remains cautious towards private sector lending. Hence, net advances witnessed shrinkage during 9MCY16. Fresh accretion in NPLs is limited. Thus asset quality was largely maintained. Deposits grew by 9%; however, concentration in top-20 depositors inched up, warranting management's attention. The bank maintained sound liquidity and good risk absorption capacity. The overall CAR has come down to 15% at end-Sep16 (end-Sep15: ~17%), a factor of rise in risk weighted assets. As part of strategy, the management intends to increase the proportion of high-quality assets in its overall mix. While it may compromise bottom-line performance, it is likely to have a positive impact on CAR.

KEY RATING DRIVERS

The rating is dependent on the bank's ability to maintain its market position in the industry while strengthening its overall risk profile. Bringing efficiency in overall operational structure is important to rationalize costs. In comparative landscape, adding granularity to core operations - deposits and advances - is critical. Meanwhile, increase in system share would be ratings positive.

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Soneri Bank Limited

PKR mln

BALANCE SHEET	30-Sep-16	31-Dec-15	31-Dec-14	31-Dec-13
Earning Assets				
Advances (Net of NPL)	96,305	109,033	105,389	94,249
Debt Instruments	3,626	2,304	1,471	854
Total Finances	99,931	111,337	106,861	95,103
Investments	121,181	106,542	74,244	45,844
Others	10,737	4,514	905	3,471
	231,849	**222,393**	**182,010**	**144,418**
Non Earning Assets				
Non-Earning Cash	18,486	16,932	16,050	12,897
Deferred Tax	-	-	-	103
Net Non-Performing Finances	2,301	2,969	2,579	3,290
Fixed Assets & Others	9,554	11,047	12,536	8,525
	30,341	**30,948**	**31,165**	**24,816**
TOTAL ASSETS	**262,189**	**253,342**	**213,175**	**169,234**
Interest Bearing Liabilities				
Deposits	201,967	185,222	163,250	140,580
Borrowings	34,622	42,876	25,825	10,485
	236,588	228,098	189,075	151,065
Non Interest Bearing Liabilities	7,338	7,052	7,061	4,886
TOTAL LIABILITIES	**243,926**	**235,150**	**196,136**	**155,951**
EQUITY (including revaluation surplus)	**18,263**	**18,192**	**17,039**	**13,283**
Total Liabilities & Equity	**262,189**	**253,342**	**213,175**	**169,234**

INCOME STATEMENT	30-Sep-16 9MCY16	31-Dec-15 Annual	31-Dec-14 Annual	31-Dec-13 Annual
Interest / Mark up Earned	13,373	18,320	16,906	13,639
Interest / Mark up Expensed	(8,114)	(10,722)	(10,626)	(8,751)
Net Interest / Markup revenue	**5,260**	**7,597**	**6,280**	**4,888**
Other Income	2,166	3,153	2,509	2,245
Total Revenue	**7,426**	**10,750**	**8,789**	**7,133**
Non-Interest / Non-Mark up Expensed	(4,833)	(6,125)	(5,798)	(4,868)
Pre-provision operating profit	2,593	4,625	2,991	2,265
Provisions	27	(1,029)	(549)	(735)
Pre-tax profit	2,620	3,596	2,442	1,529
Taxes	(1,078)	(1,383)	(860)	(494)
Net Income	**1,542**	**2,213**	**1,582**	**1,036**

Ratio Analysis	30-Sep-16	31-Dec-15	31-Dec-14	31-Dec-13
Performance				
ROE	13%	15%	12%	8%
Cost-to-Total Net Revenue	65%	57%	66%	68%
Provision Expense / Pre Provision Profit	-1%	22%	18%	32%
Capital Adequacy				
Equity/Total Assets	6%	6%	7%	7%
Capital Adequacy Ratio as per SBP	15%	15%	12%	12%
Funding & Liquidity				
Liquid Assets / Deposits and Borrowings	56%	50%	44%	40%
Advances / Deposits	49%	60%	66%	69%
CASA deposits / Total Customer Deposits	72%	69%	67%	70%
Intermediation Efficiency				
Asset Yield	8%	9%	11%	10%
Cost of Funds [Interest Expensed / Average (Deposits + Borrowings)]	5%	5%	6%	6%
Spread	3%	4%	4%	4%
Outreach				
Branches	281	266	246	239

The Pakistan Credit Rating Agency Limited

STANDARD 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. This capacity is highly unlikely to be adversely affected by foreseeable events.
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-	**Speculative.** Possibility of credit risk developing. There is a possibility of credit risk developing, particularly as a result of adverse economic change over time; however, business or financial alternatives may be available to allow financial commitments to be met.
B+ B B-	**Highly speculative.** Significant 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	**High default 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.

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 with in 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, 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, or e) the entity/issuer defaults.

Regulatory and Supplementary Disclosure

Rated Entity

Name of Issuer	Soneri Bank Limited
Name of Issue	Soneri Bank Limited | TFC
Sector	Banking
Type of Relationship	Solicited
Purpose of the Rating	Regulatory Requirement Independent Risk Assessment

Rating History

Dissemination Date	TFC	Rating Action
16-Dec-16	A+	Maintain
17-Jun-16	A+	Maintain
17-Dec-15	A+	Maintain
17-Jun-15	A+	Initial
8-May-15	A+	Initial
29-Jan-15	A+	Preliminary

Instrument Details

Nature of Instrument	Size of Issue	Tenor	Trustee	Security
TFC (Sub-ordianted, Lsited)	PKR 3,000mln	8 years	Pak Brunei Investment Company	Unsecured

Amortization Schedule See Annexure I

Related Criteria and Research

Specific Methodology: Banks Methdology - 2016
Research: Banking Sector Review - 2016

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Rating Team Statement

Rating Procedure
Rating is an opinion on relative credit worthiness of an entity or debt instrument. It does not constitute recommendation to buy, hold or sell any security. The rating team for this assignment does not have any beneficial interest, direct or indirect in the rated entity/instrument.

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Prohibition

Probability of Default (PD)

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

Regulatory and Supplementary Disclosure
Annexure I

Loan Amount (PKR)	3,000,000,000	
Tenor (Years)	8 years	
Rate	6MK + 1.35%	(Kibor assumed 6.5%)

PKR mln

Installment	Post Issuance	Principal	Mark Up	Total Installment	Outstanding
					3,000
1	Jan-16	0.6	127	128	2,999
2	Jul-16	0.6	118	118	2,999
3	Jan-17	0.6	118	118	2,998
4	Jul-17	0.6	118	118	2,998
5	Jan-18	0.6	118	118	2,997
6	Jul-18	0.6	118	118	2,996
7	Jan-19	0.6	118	118	2,996
8	Jul-19	0.6	118	118	2,995
9	Jan-20	0.6	118	118	2,995
10	Jul-20	0.6	118	118	2,994
11	Jan-21	0.6	118	118	2,993
12	Jul-21	0.6	117	118	2,993
13	Jan-22	0.6	117	118	2,992
14	Jul-22	0.6	117	118	2,992
15	Jan-23	0.6	117	118	2,991
16	Jul-23	2,991	0	2,991	0

Call option exercisable date