



The Pakistan Credit Rating Agency Limited

MCB ISLAMIC BANK LIMITED

	NEW	INITIAL
	JAN-17	FEB-16
Long-Term	A	A
Short-Term	A1	A1
Outlook	Stable	Stable

REPORT CONTENTS

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JANUARY 2017

Profile & Ownership

- MCB Islamic Bank Limited (MCBIBL) –wholly owned subsidiary of MCB banklimited - was formed as a banking company in May, 2014. It started commercial operations in November 2015.
- In April, 2016, Lahore High Court approved the demerger of Islamic Banking Group (IBG) of MCB Bank Limited (MCB) and its subsequent merger with MCBIBL.
- Resultantly, all the domestic Islamic banking operations of MCB IBG were merged into MCB IBL w.e.f September 30, 2015.
- MCBIBL has 66 branches network (as at end Dec15: 6; as at end Dec16: new 26 plus acquired through IBG: 34).
- The bank has sought permission from SBP to open another 10 branches till Dec17.
- Flexcube, the core banking software, is expected to be completely implemented by 1HCY17.
- The Bank provides a wide range of Islamic products including Ijarah, Murabha, Diminishing Musharkah, and Istisna.
- Strong presence of MCB in financial sector is likely to support MCBIBL in establishing its Islamic Banking franchise

Governance

- BoD currently comprises seven members including one MCB representatives and two independent directors. While one position is vacant.
- Mr. Ahmed Ebrahim Hasham is the acting chairman of the board.
- BoD closely monitors the management's policies and the bank's operations through its four committees, namely a) Audit Committee, b) Risk Management & Portfolio Review Committee (RM&PR) and c) Human Resource Committee and d) Business Strategy & Service Quality Control Committee.
- There is another committee Board Evaluation Committee is responsible to assess board's collective knowledge and commitment in fulfilling corporate governance responsibilities.
- M/s A.F. Ferguson & C. Chartered Accountants are the auditors of the bank.

Management

- Mr. Ali Muhammad Mahoon, President of MCBIBL, has over 20 years of experience with local and international financial institutions.
- Functional structure is followed, where the experienced top management team heads different departments.

Risk Management

- Well established Risk management function is placed. Credit risk management policies cover the qualitative and quantitative aspects of credit evaluation and monitoring. Exposure limits are adopted as per the prudential regulations.
- Designated Risk Management Group (RMG), reporting directly to RM&PR committee, takes care of risk review and adherence to the policies.
- Annual review of performance against designed metrics by RM&PR committee. Good quality morabha dominated financing portfolio (end-Sep16: 50%) followed by diminishing musharkah, Ijarah and Istisna (end- Sep16: 50%) with only one non performing client.
- Cautious lending strategy, with focus on corporate clients. However, management is heading towards other business segments including consumer financing, SME, microfinancing etc.

Performance

- During 9MCY16, MCBIBL registered a spread of 3.5%. The Bank managed to absorb its administrative costs through net revenue, while gain on sale of securities led to a profit of PKR 111mln.
- Going forward, while exploring key sectors including Cement, Fertilizer, Power, Steel, Poultry, and Sugar Industries bank is also aiming to explore new business segments including consumer financing, Microfinancing and digital banking etc.

Funding & Capital

- Post merger deposits size exhibited a growth of 49% (end-Sep16: PKR 14,099mln; end Dec15 (merged): PKR 9,450mln). MCBIBL's management is targeting to grow its deposit base to ~PKR 21 bln by end-Dec17.
- CASA remained at 60% as at end Sep16.
- The bank has already met the Minimum Capital Requirement (MCR) of PKR6bln through capital injection worth PKR 10bln from the parent - MCB.

RATING RATIONALE

MCB Islamic Bank is a wholly owned subsidiary of MCB Bank Limited. MCB Bank has long-term rating of "AAA" reflecting its robust profile duly supplemented by its strong market position in local banking landscape, established brand equity, and sound financial profile. As per envisaged strategy to consolidate Islamic banking operations, Islamic Banking Group (IBG) operations of MCB were merged with MCBIBL; the related process has recently been completed. The effective date of merger stands September 30, 2015. This has given a boost to stand-alone operational profile of MCBIBL. Meanwhile, the management continues to follow its conservative business strategy, while gradually building a sound assets book and a diversified deposit base. The bank is in the process of establishing its operational infrastructure including branch network, technology implementation, and its risk management framework, besides continuing improvements in governance structure. The ratings incorporate inherent constraints faced by MCBIBL, mainly limited branch network, small deposit base, and high cost structure particularly in early years.

KEY RATING DRIVERS

Islamic banking industry offers healthy growth opportunities. However, MCBIBL's prospects are dependent upon the management's ability to establish its position. Effective implementation of business strategy is important.



BALANCE SHEET	30-Sep-16	31-Dec-15	31-Dec-15
	9MCY16	(Restated after merger) Annual	(Change of Y/E to Dec) Annual
Earning Assets			
Financing	14,427	12,569	973
Private Sukuks	2,015	2,052	(39)
Total Financing	16,442	14,621	933
Investments	5,286	3,962	664
Others	4,565	6,277	8,132
	26,293	24,860	9,729
Non Earning Assets			
Non-Earning Cash	1,848	769	76
Deferred Tax	-	-	9
Net Non-Performing Financing	(151)	(95)	-
Fixed Assets & Others	2,046	1,364	294
	3,743	2,038	379
TOTAL ASSETS	30,035	26,898	10,108
Remunerative Liabilities			
Deposits	14,099	9,450	38
Borrowings	5,015	632	-
	19,114	10,082	38
Non-remunerative Liabilities	886	6,839	86
TOTAL LIABILITIES	20,000	16,921	124
EQUITY (including revaluation surplus)	10,036	9,977	9,984
Total Liabilities & Equity	30,035	26,898	10,108
INCOME STATEMENT	30-Sep-16	30-Sep-15	31-Dec-15
	9MCY16	9MCY15	(Change of Y/E to Dec) Annual
Profit / Return Earned	1,203	41	155
Return Expensed	(419)	-	(0)
Net Revenue	784	41	155
Other Income	211	-	11
Total Revenue	995	41	166
Admin and Other Expenses	(752)	(6)	(113)
Pre-provision operating profit	242	35	53
Provisions	(56)	-	-
Pre-tax profit	186	35	53
Taxes	(76)	-	(5)
Net Income	111	35	48

Note: Dec15 Profit and Loss Statement is not available.



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.

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

<p>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.</p>	<p>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’.</p>	<p>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.</p>	<p>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.</p>
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Disclaimer: PACRA's rating is an assessment of the credit standing of an entity/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.



Name of Rated Entity
Sector
Type of Relationship

MCB Islamic Bank Limited
Banking
Solicited

Purpose of the Rating

Regulatory Requirement
Independent Risk Assessment

Rating History

Dissemination Date	Long Term	Short Term	Outlook	Action
01-Feb-16	A	A1	Stable	Initial

Related Criteria and Research

Applicable Criteria and
Rekated Reseach

Banking Rating Methodology
Islamic Banking Sector - Viewpoint | Feb-16

Rating Analysts

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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.

Disclaimer

Rating Shopping

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Surveillance

PACRA monitors all the outstanding ratings continuously and any potential change therein due to any event associated with the rated entity/ issuer, the security

arrangement, the industry etc, is disseminated to the market, in a timely and effective manner, after appropriate consultation with the entity/issuer

PACRA reviews all the outstanding ratings on annual basis or as and when required by any stakeholder (including creditor) or upon the occurrence of such an event which requires to do so

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

Reporting of Misconduct

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

relating to the credit rating by another employees of the company that came to his/her knowledge. The Compliance Officer reports to the BoD and SECP

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