The Pakistan Credit Rating Agency Limited

SONERI BANK LIMITED
RATING REPORT

	NEW [DEC-17]	PREVIOUS [JUN-17]
Entity		
Long Term	AA-	AA-
Short Term	A1+	A1+
Outlook	Stable	Stable

REPORT CONTENTS

DECEMBER 2017

Profile & Ownership

- Soneri Bank Limited (SBL), incorporated in Sep91, has a sustained deposit system share of 1.8%
- At end-Sep17, bank is operating with a network of 286 branches (CY16: 288, CY15: 266) across the country
- Feerasta Family – sponsors of Rupali Group – holds controlling stake (58%), followed by NIT (~10%), while rest is spread across general public and others

Governance & Management

- Eight member board including the CEO; three directors represent Feerasta Family, one is NIT nominee, while three are independent members
- The President and CEO, Mr. Aftab Manzoor, carries over three decades of international banking experience. Executive Director and COO, Mr. Amin A. Feerasta, has been associated with the bank since 2000.
- Operations divided into sixteen functions

Risk Management

- During 9MCY17, lending portfolio registered 25% growth with corporate and SME segment dominating the portfolio
- The bank's advances to deposit ratio surged to 72.5% (CY16: 59%) on account of greater increase in lending
- Top-20 performing exposure's concentration witnessed marginal improvement to 22% (CY16: 23%)
- During 9MCY17, infection ratio declined to 6.3% (CY16: ~8%) on back of significant increase in gross advances; NPLs remained largely same
- Investment portfolio, comprising 43% of earning assets, witnessed 14% growth in the period; dominated by government securities (97%); mix tilted towards T-bills

Business Risk

- During 9MCY17, net interest income witnessed decline (22%), despite significant rise in earning assets (21%); mark-up expenses also inched up. Hence, spread marginally reduced to 2.4% (CY16: 2.9%)
- Non-markup income increased to PKR 2.5bln, up 17% YoY
- Operating expenses (cost to total net revenue) increased to ~71% in 9MCY17 (CY16: ~68%)
- During 9MCY17, the provisioning expense increased to PKR 100mln, the profit after tax stood at PKR 1.2bln, down 20% YoY
- Going forward, management is focused on low cost deposit mobilization and capitalizing on CPEC opportunities through participation in consortiums

Financial Risk

- At end-Sep17, deposits stood at PKR 202bln with an increase of 2% - industry witnessed growth of 7%; CASA improved to ~72% (end-Dec16: ~70%, end-Dec15: 69%)
- Top-20 depositors' concentration remained at 25% (CY16: 25%); considered high when compared with AA rating benchmarks.
- Overall liquidity position declined significantly to ~34% (end-Dec16: 47%, end-Dec15: 50%).
- CAR stood at 13.0% (Tier-I: end-Sep17: 10.3%, end-Dec16: 10.8%) declined YoY; owing to decrease in profitability and significant rise in risk weighted assets

TFC Issue:

- SBL issued 2nd subordinated, unsecured, and listed TFC of PKR 3,000mln in Jul15 (Tenor 8 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 and loss absorbency clauses
- Cushion to loss absorbency ranges from 3% to 5% after incorporation of projections

RATING RATIONALE

The ratings reflect Soneri Bank's sustained business profile; system share remained intact YoY. There was a meager increase in deposit base - lower than average industry. The bank continues to make fresh deployment in advances, hence an increase was witnessed in the bank's ADR - which is comparatively higher than industry average. The reduction in net interest revenue translated into reduced profitability YoY, a factor of squeeze in spreads – an industry wide phenomenon. Going forward, the bank, while focusing to improve asset quality, intends to follow a prudent strategy in terms of advances growth. Enhancing non-fund based exposure, in turn fee income and would be targeted while capitalizing on potential business opportunities expected from China-Pakistan Economic Corridor. At the same time, the strategy would be to mobilize low-cost deposits with an increase in branch network. The bank's CAR reduced to 13.0% (end-Dec16: 14.1%) primarily on account of increase in risk weighted assets.

KEY RATING DRIVERS

The rating is dependent on the bank's ability to maintain its market position in banking 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, sustainable increase in system share and consequent profitability would be ratings positive.

Soneri Bank Limited

PKR mln

BALANCE SHEET	30-Sep-17	31-Dec-16	31-Dec-15	31-Dec-14
	9MFY17	Annual	Annual	Annual
Earning Assets				
Advances (Net of NPL)	154,054	123,333	109,033	105,389
Debt Instruments	2,894	3,989	2,304	1,471
Total Finances	156,948	127,322	111,337	106,861
Investments	130,066	113,895	106,542	74,244
Others	11,741	5,678	4,514	905
	298,755	**246,894**	**222,393**	**182,010**
Non Earning Assets				
Non-Earning Cash	19,753	18,960	16,932	16,050
Deferred Tax	-	-	-	-
Net Non-Performing Finances	1,797	1,972	2,969	2,579
Fixed Assets & Others	10,901	10,693	11,047	12,536
	32,451	**31,625**	**30,948**	**31,165**
TOTAL ASSETS	**331,206**	**278,520**	**253,342**	**213,175**
Interest Bearing Liabilities				
Deposits	214,846	210,840	185,222	163,250
Borrowings	90,576	41,903	42,876	25,825
	305,422	252,743	228,098	189,075
Non Interest Bearing Liabilities	8,663	7,488	7,052	7,061
TOTAL LIABILITIES	**314,085**	**260,230**	**235,150**	**196,136**
EQUITY (including revaluation surplus)	**17,121**	**18,289**	**18,192**	**17,039**
Total Liabilities & Equity	**331,206**	**278,520**	**253,342**	**213,175**

INCOME STATEMENT	30-Sep-17	31-Dec-16	31-Dec-15	31-Dec-14
	9MFY17	Annual	Annual	Annual
Interest / Mark up Earned	13,653	17,524	18,320	16,906
Interest / Mark up Expensed	(8,748)	(10,680)	(10,722)	(10,626)
Net Interest / Markup revenue	**4,906**	**6,844**	**7,597**	**6,280**
Other Income	2,530	2,736	3,150	2,509
Total Revenue	**7,436**	**9,580**	**10,748**	**8,789**
Non-Interest / Non-Mark up Expensed	(5,236)	(6,479)	(6,123)	(5,798)
Pre-provision operating profit	2,199	3,102	4,625	2,991
Provisions	(100)	(24)	(1,029)	(549)
Pre-tax profit	2,100	3,077	3,596	2,442
Taxes	(868)	(1,198)	(1,383)	(860)
Net Income	**1,231**	**1,879**	**2,213**	**1,582**

Ratio Analysis	30-Sep-17	31-Dec-16	31-Dec-15	31-Dec-14
Performance				
ROE	10.3%	12.0%	15.0%	11.9%
Cost-to-Total Net Revenue	70.6%	67.8%	57.3%	66.2%
Provision Expense / Pre Provision Profit	4.5%	0.8%	22.3%	18.4%
Capital Adequacy				
Equity/Total Assets	4.8%	5.7%	6.1%	6.6%
Capital Adequacy Ratio as per SBP	13.0%	14.1%	15.4%	12.5%
Funding & Liquidity				
Liquid Assets / Deposits and Borrowings	33.7%	47.5%	50.0%	44.4%
Advances / Deposits	72.5%	59.4%	60.5%	66.1%
CASA deposits / Total Customer Deposits	71.8%	69.9%	69.2%	67.2%
Intermediation Efficiency				
Asset Yield	6.8%	7.6%	9.2%	10.5%
Cost of Funds [Interest Expensed / Average (Deposits + Borrowings)]	4.4%	4.7%	5.4%	6.3%
Spread	2.4%	2.9%	3.8%	4.2%
Outreach				
Branches	286	288	266	246

CREDIT 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.
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

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