RATING REPORT

Faysal Bank Limited

REPORT DATE:
June 30, 2021

RATING ANALYST:
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RATING DETAILS				
Rating Category	**Latest Rating**		**Previous Rating**	
	Long-term	**Short-term**	**Long-term**	**Short-term**
Entity Rating	AA	A-1+	AA	A-1+
Outlook	Stable		Stable	
Date	*June 30, '21*		*June 29, '20*	

COMPANY INFORMATION	
Established in 1994	**External auditors:** A.F. Ferguson & Co. Chartered Accountants
Public Limited Company	**Chairman of the Board:** Mr. Farooq Rahmatullah
Key Shareholders (with stake 5% or more):	**CEO:** Mr. Yousaf Hussain
Ithmaar Bank B.S.C ~48.06%	
Faisal Finance (Luxemborg) S.A. ~8.55%	
MFAI (Jersey) Limited ~5. 89%	
State Life Insurance Corporation of Pakistan ~5.30%	
General Public ~14.6%	

APPLICABLE METHODOLOGY(IES)
VIS Commercial Banks Rating: **https://s3-us-west-2.amazonaws.com/backupsqlvis/docs/Meth-CommercialBanks202006.pdf**

Faysal Bank Limited

OVERVIEW OF THE INSTITUTION

Ithmaar Bank B.S.C (IB), an Islamic Retail Bank in Bahrain and Kuwait, is the parent Bank of Faysal Bank Limited, holding directly and indirectly, 66.8% of FBL's shares.

FBL has a branch network of 576 branches (2019: 555); including 500 Islamic branches in Pakistan.

Profile of Chairman

Mr. Farooq Rahmatullah is a seasoned professional with a diverse experience in several roles in different organizations. He is a Law graduate and is currently serving on Board of three other organizations.

Profile of CEO

Mr. Yousaf Hussain has over 27 years of professional experience, primarily at ABN AMRO Bank where he held multiple senior managerial positions including those within the Corporate / Credit and Transaction Banking functions. He has been affiliated with Faysal Bank since August 2008, with a significant contribution to the franchise in his previous positions as Chief Risk Officer.

RATING RATIONALE

Faysal Bank Limited (FBL) is a mid-sized Bank with Ithmaar Bank B.S.C (an Islamic Retail Bank in Bahrain and Kuwait) being the sponsor Bank holding directly and indirectly major shareholding. FBL is engaged in provision of banking services in Pakistan for 27 years and caters to all customer segments, i.e. Retail, SMEs, Commercial, Agri-based and Corporates. Headquartered in Karachi, the Bank's footprint spreads over 207 cities across Pakistan with 576 (2019: 555) branches; of which 87% (500 branches) are currently dedicated for Islamic banking and further expansion of the Islamic network is underway.

Management remains committed to convert into a full-fledged Shariah compliant Bank in a financially prudent manner.

At end-2020, total Sharia compliant deposits as proportion of total deposits increased to 46% (2019: 26%) on the back of two-fold increase in Islamic deposits. On advances front, the Bank managed to achieve the conversion target of two-third (67%) of financing portfolio under Islamic modes as at end-1Q'21. Going forward, the Bank plans to continue its aggressive conversion to Islamic with new consumer finance products planned to be launched in the ongoing year.

In 2020, FBL added 21 (2019: 100) new branches and converted 65 (2019: 59) conventional branches to Islamic including 5 flagship branches. Over the last two years, Islamic branch network has almost doubled, reaching to 500 branches in 2020 (compared to 254 branches in 2018). The management plans to convert another 66 conventional branches to Islamic along with the addition of 30 new Islamic branches during 2021.

Asset growth was concentrated in investments in 2020 and in the ongoing year. Financing portfolio registered a nominal growth given prudent lending strategy amid Covid-19 led macroeconomic uncertainties.

Asset growth in 2020 was mainly driven by deposit growth which was channeled primarily towards the investment portfolio. On a timeline basis, the asset mix depicts a rising trend in investments, thus resulting in ADR declining to ~52% in 1Q'21 from 68% in 2019.

FBL's gross financing portfolio registered a nominal growth of ~2% (vis-à-vis industry growth of ~4%). Prudent lending strategy amid uncertain macroeconomic environment led to subdued portfolio growth as credit demand remained muted. However, market share (in terms of gross advances) remains intact at ~4.2%. Largest quantum of incremental financing in 2020 was extended to power, textile, transport and service sector; all represented one-half of gross lending portfolio. Corporate financing continues to remain the forte of the bank as it constitutes the largest proportion (~80%) of total lending portfolio. Client wise concentration in advances has witnessed considerable improvement on a timeline basis. Lending to the private sector represents the major portion of the financing portfolio with the same accounting for four-fifth of loan book.

Operational strategy amidst Covid-19 and update on deferments/restructuring cases.
In response to the pandemic, FBL carried out an overall and segment level testing in the April'20 and July'20 whereby individual customers are categorized as high, medium and low. The management also updated ORRs of each customer based on the potential risk of default while broad review of credit portfolio on monthly basis is now being ensured.

FBL accepted 10,519 applications for deferments/ restructuring due to Covid-19 pandemic; 136 cases are still under review. Of total approved cases 5,550 were related to principal deferment (amounting to Rs. 25.6b for one year) while remaining were for loan restructuring (principal restructuring of Rs. 5.3b and markup adjustment of Rs. 818m).

Asset quality indicators remain sound in 2020. Going forward, credit risk emanating from loan book would remain elevated due to possible headwinds that might arise post expiry of Covid-19 deferments/restructuring.
Asset quality indicators of the Bank remain sound while provisioning coverage increased at end-2020. Overall gross and net infection ratios have noted improvement which is due to significant write-offs (pertaining to previously provisioned loans) of Rs. 4.9b in 2020 and Rs. 1.7b in 1Q'21. Provisioning is expected to remain elevated primarily due to higher NPLs expected (given sizeable exposure in one major high risk oil and gas client) and change in classification of existing NPLs (as around 85% of NPLs were classified as loss as at end-1Q'21). Going forward, credit risk emanating from loan book would remain elevated due to possible headwinds that might arise post expiry of Covid-19 deferments/restructuring. However, comfort is drawn from a gradual revival in the overall global economy along with improved domestic macro-economic sentiments.

Sizeable increase observed in investment portfolio with majority deployment in long-term Ijara Sukuk and PIBs. Conversion of investment portfolio into Islamic with similar conventional yields remains a challenge for the Bank.
Net investment portfolio, after registering a 36% growth in 2020, increased by 13% to reach Rs. 313.9b (2020: Rs. 276.9b) at end-1Q'21. Credit risk emanating from investment portfolio remains limited as three-fourth of investments are deployed in GoP securities. While T-Bills continued to represent the major share in investments, the portfolio witnessed a shift and major chunk of the fresh liquidity was deployed in long-term Ijara Sukuk and PIBs during 2020. However, given the uncertainty with regards to benchmark rates, preferred investment avenue of the Bank remains short tenor instruments. Going forward, conversion of investment portfolio into Islamic with similar yields to conventional remains a challenge for the Bank as at present there is no active market for privately placed Sukuks and no regular issuance of GoP Ijarah Sukuks (largely due to non-availability of unencumbered assets and major public financing being arranged from conventional banks).

Liquidity profile remains comfortable; sizeable deposit growth witnessed while concentration has room for improvement.
Liquidity profile has witnessed improvement on account of increase in liquid assets in relation to total deposits and borrowings (adjusted for repo) on a timeline basis (1Q'21: 62.1%; 2020: 54.1%; 2019: 48.5%). The bank also maintains considerable cushion over the regulatory requirements of Liquidity Coverage Ratio (LCR) and

Net Stable Funding Ratio (NSFR). Deposit base grew by ~18% (vis-à-vis industry's domestic deposit growth of 16%) in 2020 while market share remained around 3%. The growth largely emanated from higher average growth in low-cost saving and current deposits (CASA) and was further supported by lesser spending by various sectors and individuals given the slowdown in economy due to Covid-19. CASA deposits in 2020 have grown by ~20%. The same has been increasing on a timeline basis and was reported at 73.6% (2020 71.1%; 2019: 70.1%; 2018: 68.2%) in 1Q'21.

Deposit concentration, despite depicting improvement on a timeline basis, remains on the higher side with Top-50 depositors representing around one-fourth of total deposits. Individual deposits stood around 23.9% (2019: 27.9%) of deposit base while number of customers registered an increase of 10% in 2020 and reached at 852K.

Despite significant higher provisioning, profitability profile continues to witness improvement.
Despite a steep decline in benchmark rates, net interest income increased by 16% in 2020 which was largely driven by spread improvement. The decrease in cost of deposits was higher than the decline in average return on earning assets, thus resulting in improvement of spreads. Cost-to-income ratio is maintained at around 60.0% (2020: 59.2%; 2019: 60.1%) in 1Q'21. Bottom-line profitability grew by ~ 8% in 2020 despite higher provisioning charges to the tune of Rs. 2.2b (2019: Rs. 0.8b).

Profit retention has noticeably strengthened capitalization over the years; the same is expected to maintain cushion over the regulatory requirement
Equity (excluding revaluation surplus) has depicted increase on a timeline basis on account of profit retention and no dividend payout since 2017. Capital Adequacy Ratio (CAR) improved to 19.5% (2020: 18.7%) whereas leverage ratio declines slightly to 5.8% (2020: 5.9%) respectively. Going forward, capitalization indicators are expected to demonstrate comfortable cushion over the regulatory requirements despite accounting for IFRS 9 accounting standards.

FINANCIAL SUMMARY Appendix I

BALANCE SHEET *(Figures in PKR Billions)*	Dec 31, 2018	Dec 31, 2019	Dec 31, 2020	Mar 31, 2021
Investments	214	204	277	314
Advances	296	310	318	322
Total Assets	600	630	710	750
Borrowings	98	73	58	91
Deposits & other accounts	409	458	541	549
Issued, subscribed and paid up capital	15	15	15	15
Tier-1 Equity	37	43	50	52
Net Worth	43	55	60	62
INCOME STATEMENT *(Figures in PKR millions)*				
Net Mark-up Income	16,275	21,120	24,535	5,439
Net Provisioning/(Reversal)	(422)	843	2,254	(533)
Non-Markup Income	6,584	7,170	8,231	2,226
Operating Expenses	14,816	17,068	19,401	4,608
Profit Before Tax	8,202	10,192	10,771	3,513
Profit After Tax	4,837	6,041	6,512	2,103
RATIO ANALYSIS				
Market Share (Advances) (%)	4.1%	4.1%	4.0%	4.0%
Market Share (Deposits) (%)	3.1%	3.1%	3.0%	3.1%
Gross Infection (%)	8.3%	9.1%	7.7%	6.9%
Provisioning Coverage (%)	89.2%	79.7%	82.2%	83.2%
Net Infection (%)	1.2%	2.2%	1.7%	1.5%
Cost of funds (%)	4.4%	7.2%	5.2%	3.7%
Net NPLs to Tier-1 Capital (%)	9.5%	15.8%	11.0%	9.1%
Capital Adequacy Ratio (C.A.R (%))	16.8%	19.1%	18.7%	19.5%
Markup Spreads (%)	3.3%	4.6%	4.7%	3.9%
Efficiency (%)	66.5%	60.1%	59.2%	60.0%
Basic* ROAA (%)	1.4%	1.8%	1.7%	1.4%
ROAA (%)	0.9%	1.0%	1.0%	1.2%
ROAE (%)	13.4%	14.6%	13.6%	16.1%
Liquid Assets to Deposits & Borrowings (%)	53.6%	48.5%	54.1%	62.1%

ISSUE/ISSUER RATING SCALE & DEFINITIONS Appendix II

VIS Credit Rating Company Limited

RATING SCALE & DEFINITIONS: ISSUES / ISSUERS

Medium to Long-Term

AAA
Highest credit quality; the risk factors are negligible, being only slightly more than for risk-free Government of Pakistan's debt.

AA+, AA, AA-
High credit quality; Protection factors are strong. Risk is modest but may vary slightly from time to time because of economic conditions.

A+, A, A-
Good credit quality; Protection factors are adequate. Risk factors may vary with possible changes in the economy.

BBB+, BBB, BBB-
Adequate credit quality; Protection factors are reasonable and sufficient. Risk factors are considered variable if changes occur in the economy.

BB+, BB, BB-
Obligations deemed likely to be met. Protection factors are capable of weakening if changes occur in the economy. Overall quality may move up or down frequently within this category.

B+, B, B-
Obligations deemed less likely to be met. Protection factors are capable of fluctuating widely if changes occur in the economy. Overall quality may move up or down frequently within this category or into higher or lower rating grade.

CCC
Considerable uncertainty exists towards meeting the obligations. Protection factors are scarce and risk may be substantial.

CC
A high default risk

C
A very high default risk

D
Defaulted obligations

Short-Term

A-1+
Highest certainty of timely payment; Short-term liquidity, including internal operating factors and /or access to alternative sources of funds, is outstanding and safety is just below risk free Government of Pakistan's short-term obligations.

A-1
High certainty of timely payment; Liquidity factors are excellent and supported by good fundamental protection factors. Risk factors are minor.

A-2
Good certainty of timely payment. Liquidity factors and company fundamentals are sound. Access to capital markets is good. Risk factors are small.

A-3
Satisfactory liquidity and other protection factors qualify entities / issues as to investment grade. Risk factors are larger and subject to more variation. Nevertheless, timely payment is expected.

B
Speculative investment characteristics; Liquidity may not be sufficient to ensure timely payment of obligations.

C
Capacity for timely payment of obligations is doubtful.

Rating Watch: VIS places entities and issues on 'Rating Watch' when it deems that there are conditions present that necessitate re-evaluation of the assigned rating(s). Refer to our 'Criteria for Rating Watch' for details. www.vis.com.pk/images/criteria_watch.pdf

Rating Outlooks: The three outlooks 'Positive', 'Stable' and 'Negative' qualify the potential direction of the assigned rating(s). An outlook is not necessarily a precursor of a rating change. Refer to our 'Criteria for Rating Outlook' for details.www.vis.com.pk/images/criteria_outlook.pdf

(SO) Rating: A suffix (SO) is added to the ratings of 'structured' securities where the servicing of debt and related obligations is backed by some sort of financial assets and/or credit support from a third party to the transaction. The suffix (SO), abbreviated for 'structured obligation', denotes that the rating has been achieved on grounds of the structure backing the transaction that enhanced the credit quality of the securities and not on the basis of the credit quality of the issuing entity alone.

(blr) Rating: A suffix (blr) is added to the ratings of a particular banking facility obtained by the borrower from a financial institution. The suffix (blr), abbreviated for 'bank loan rating' denotes that the rating is based on the credit quality of the entity and security structure of the facility.

'p' Rating: A 'p' rating is assigned to entities, where the management has not requested a rating, however, agrees to provide informational support. A 'p' rating is shown with a 'p' subscript and is publicly disclosed. It is not modified by a plus (+) or a minus (-) sign which indicates relative standing within a rating category. Outlook is not assigned to these ratings. Refer to our 'Policy for Private Ratings' for details. www.vis.com.pk/images/policy_ratings.pdf

'SD' Rating: An 'SD' rating is assigned when VIS believes that the ratee has selectively defaulted on a specific issue or obligation but it will continue to meet its payment obligations on other issues or obligations in a timely manner.

REGULATORY DISCLOSURES	Appendix III
Name of Rated	Faysal Bank Limited
Sector	Commercial Banks
Type of Relationship	Solicited
Purpose of Rating	Entity Rating

Rating History

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
RATING TYPE: Entity				
30-Jun-21	AA	Stable	A-1+	Reaffirmed
29-Jun-20	AA	Stable	A-1+	Reaffirmed
27-Jun-19	AA	Stable	A-1+	Reaffirmed
29-Jun-18	AA	Stable	A-1+	Reaffirmed
30-Jun-17	AA	Stable	A-1+	Reaffirmed
28-Jun-16	AA	Stable	A-1+	Reaffirmed
30-Jun-15	AA	Stable	A-1+	Reaffirmed
30-Jun-14	AA	Stable	A-1+	Reaffirmed
26-Jun-13	AA	Stable	A-1+	Reaffirmed
02-Jul-12	AA	Stable	A-1+	Reaffirmed
28-Jun-11	AA	Stable	A-1+	Reaffirmed
24-Feb-11	AA	Stable	A-1+	Rating Watch Removed
01-Jun-10	AA		A-1+	Rating Watch - Developing

Instrument Structure	N/A
Statement by the Rating Team	VIS, the analysts involved in the rating process and members of its rating committee do not have any conflict of interest relating to the credit rating(s) mentioned herein. This rating is an opinion on credit quality only and is not a recommendation to buy or sell any securities.
Probability of Default	VIS ratings opinions express ordinal ranking of risk, from strongest to weakest, within a universe of credit risk. Ratings are not intended as guarantees of credit quality or as exact measures of the probability that a particular issuer or particular debt issue will default.
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Due Diligence Meetings Conducted

S.no	Name	Designation	Date
1	Mr. Syed Majid Ali	Chief Financial Officer	June 21, 2021
2	Mr. Yousaf Hussain	Chief Executive Officer	June 28, 2021