SILKBANK LIMITED

Chairman: Mr. Munnawar Hamid OBE; President & CEO: Mr. Azmat Tarin

July 05, 2013

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Category	Latest	Previous*
Entity	A-/A-2 *Jun 29, '13*	A-/A-3 *Oct 22,'12*
Outlook	*Stable* *Jun 29, '13*	*N/A* *Oct 22, '12*

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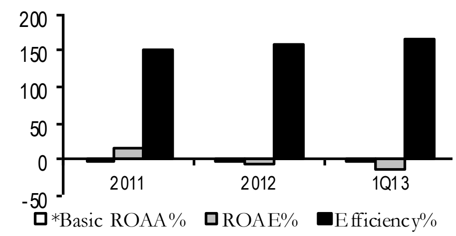
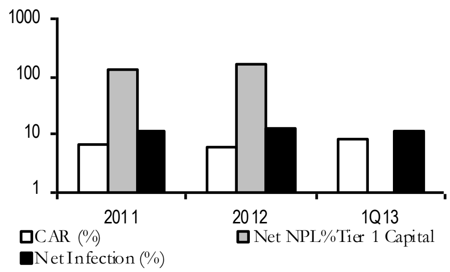
Key Financial Trends



** based on recurring profit before provision and taxation*



	2011	2012	1Q13
Total Assets (Rs. In b)	90.7	89.1	93.9
Net Advances (Rs. in b)	49.9	49.0	51.2
Deposits (Rs.in b)	64.1	69.1	69.1
Market Share (%)	1.09	1.03	1.02
Deposit Cost (%)	8.2	7.5	6.3
Profit / (Loss) (Rs.in m)	695	(344)	(219)
Equity (Rs. in b)	5.6	5.4	7.4
CAR (%)	6.6	5.7	8.3
Liquid Assets % Deposits & Borrowings	19%	20%	22%
Net Infection (%)	11.5	12.1	11.6

Rating Rationale

With issuance of Non-cumulative Convertible Preference Shares (PNCPS) in March 2013, fresh capital of Rs. 2.2b has been injected in Silk Bank Limited (Silk); net equity of the bank by end-Mar'13 was higher at Rs. 7.2b. Given that PNCPS are considered CAR eligible instruments by the State Bank of Pakistan (SBP), CAR of the bank improved to 8.25% by end-Mar'13. The bank has solicited approval from SBP for eligibility of PNCPS for meeting the Minimum Capital Requirement (MCR); response on the same is awaited. As per SBP's directive, banks are required to meet MCR of Rs. 10b and CAR of 10% by December 31, 2013. With increase in net equity of the bank, net NPLs to equity of the bank has declined on a timeline basis; it is however still sizeable at 103% at end-Mar'13. The bank is projecting additional recoveries during the on-going year. Achievement of the target is considered important for reinstating the risk profile of the bank.

Liquid assets in relation to deposits and borrowings of the bank were around 22% at end-Mar'13. Liquidity cushion maintained by the bank is on the lower side, given that top ten deposits represent 19% (FY11: 18%) of deposit base; maturity mismatch in assets and liabilities is also significant. Some improvement in liquid assets has been witnessed subsequent to Mar'13. Liquid reserves in relation to deposits & borrowings may be augmented further to maintain a comfortable liquidity position. Moreover, maturity of sizeable high-cost TDRs in 2013 is expected to have a positive impact on cost of deposits of the bank. Growth momentum has been witnessed in deposit mobilization under recently launched Islamic banking operations; continuance of the same may also positively impact the cost of deposit of the bank.

Gross advances of the bank declined slightly to Rs. 54b (FY11: Rs. 55b) by end-2012. While fresh NPLs have arisen in 2012, recoveries during the year have slightly reduced NPLs to Rs. 10.8b (FY11: Rs. 11b). Corporate, SME and consumer segments have witnessed fresh accretion in NPLs in 2012. Corporate segment represents the largest business segment with a share of 42% (FY11: 46%); share of consumer and SME has increased to 6% and 24%, respectively. Over the past one year, to strengthen the risk profile of the portfolio, focus in corporate segment has been on structured loans as opposed to evergreen lines. In consumer and SME, over the past 2-3 years, fresh lending has been undertaken under Personal Installment Loan (PIL), Ready Line (RL) and M'Power, representing 13% of total advances. NPLs have risen in PIL on a timeline basis; management is pro-actively tracking portfolio quality. NPLs have also arisen in SME – secured lending product M'power, with higher gross infection of 10.5% (FY11: 6.9%) at end-Dec'12.

With the maturity of legacy PIBs portfolio, exposure of the bank to interest rate risk has diminished significantly. Proportion of equities has increased in the investment portfolio to 11% (FY11: 4%), mostly on account of shares acquired in lieu of debt restructuring of clients.

Achievement of operational break-even on a monthly basis has extended beyond the initial envisaged timeline. Silk reported loss before taxation of Rs. 529m for FY12. Operational loss of the bank for FY12 was Rs. 1.5b (FY11: Operational loss of Rs. 1.2b) which was off-set by recoveries against NPLs. While pace of recoveries has remained strong, given that considerable time and effort is required to redeploy OREO properties as earning assets, the bank has not been able to fully realize the benefit of recoveries upfront. Efforts in this respect are however also on-going with sale of Rs. 1.5b of OREO properties achieved to-date against full year target of Rs. 3.5b. Profitability of the bank has remained under stress on account of high cost base and sizeable proportion of non-earning assets. Infusion of equity in the on-going year and sale of OREO properties is likely to have a positive impact on earnings capacity.

Overview of the Institution

Silk is listed on all three stock exchanges of Pakistan. International Finance Corporation, Nomura European Investment Limited, Bank Muscat S.A.O.G and executives of Sinthos Capital Advisors Limited had aggregate share of 82.2% in the bank at end-Dec'12. External auditors of the bank for 2012 were KPMG Taseer Hadi & Co. For 2013, Deloitte Yousuf Adil & Saleem have been appointed as external auditors JCR-VIS