RATING REPORT

Habib Bank Limited

REPORT DATE:
June 30, 2021

RATING ANALYSTS:
Asfia Aziz
asfia.aziz@vis.com.pk

RATING DETAILS				
	Latest Rating		Previous Rating	
Rating Category	**Long-term**	**Short-term**	**Long-term**	**Short-term**
Entity Rating	AAA	A-1+	AAA	A-1+
TFC	Redeemed		AAA	
TFC (ADT-1)	AA+		AA+	
Outlook	Stable		Stable	
Date	*June 30, 2021*		*June 30, 2020*	

COMPANY INFORMATION	
Established in 1941	**External auditors:** KPMG Taseer Hadi & Co.
Public Limited Company	**Chairman of the Board:** Mr. Sultan Ali Allana
Key Shareholders (with stake of 5% or more):	**President & CEO:** Mr. Muhammad Aurangzeb
Aga Khan Fund for Economic Development – 51.00%	

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

Habib Bank Limited

OVERVIEW OF THE INSTITUTION	RATING RATIONALE

OVERVIEW OF THE INSTITUTION

Habib Bank Limited (HBL) was established as a privately held bank in 1941. Currently the Bank operates as a public limited company with majority shareholding held by the Aga Khan Fund for Economic Development (AKFED).

Profile of Chairman

Mr. Sultan Ali Allana has served as the Chairman of the Board of Directors of HBL since February 2004. He has over 36 years of experience in the financial and banking sector. Mr. Allana also serves on the Boards of several institutions.

Profile of CEO

Mr. Muhammad Aurangzeb joined HBL on April 30, 2018 as the President & CEO of the Bank. Mr. Aurangzeb possesses an overall banking experience of more than 30 years in both domestic and international locations. He has held senior positions in ABN AMRO Bank and Royal Bank of Scotland and was Chief Executive Officer – Global Corporate Bank, Asia

RATING RATIONALE

Largest commercial bank with systemic importance and diversified operations.

Habib Bank Limited (HBL) is the largest commercial bank in the country with market share (based on domestic deposits) remaining consistently over 14%. HBL enjoys strong domestic operations and franchise with systemic importance to the domestic financial sector. The Bank through its subsidiaries and associates has a presence in the Insurance (Jubilee Life and Jubilee General are amongst the leading insurance companies in the country), Asset Management (HBL AMC) and Microfinance (First Microfinance Bank is the second largest microfinance bank in the industry) sectors as well.

Pace of credit growth slowed down in 2020 but has remained in line with industry growth. Asset quality indicators of the bank remain sound with increased provisioning coverage amidst uncertain economic environment.

Major portion of the Bank's assets comprises exposure to sovereign/public sector. Aggregate exposure to Sovereign and the public sector by way of investments & advances represented around 58.5% (2019: 52.4%) of total assets at end-2020. Investments continue to represent the largest chunk of the asset base contributing 52% (2019: 44%) at end-Dec'20 with growth in the same outpacing growth in advances. Resultantly, proportion of advances in total assets declined to 31% (2019: 35%) at end-2020. Prudent lending strategy amid uncertain macroeconomic environment led to subdued portfolio growth as credit demand remained muted. Largest sectoral exposures remained in power and textile sectors and both these sectors have performed well. Given HBL's dominant share in private sector credit, the proportion of private sector financing to total gross advances stood at 77% (2019: 74%) at end-2020. Segment-wise financing mix has largely remained unchanged with corporate financing representing the largest segment. During 2020, credit contraction was noticed in retail, commercial and commodity segments with corporate, consumer and rural segments witnessing growth of 9%, 25% and 10%, respectively. Despite growth, infection in the consumer portfolio remains well below industry norms.

Asset quality indicators remain sound while provisioning coverage increased at end-2020 in view of potential credit impairments from the economic effects of the pandemic. The exposure of the banking sector to credit risk is elevated due to COVID-19. However, comfort is drawn from a gradual revival in the overall global economy in the ongoing year along with sufficient provisioning coverage against possible headwinds that might arise post expiry of COVID deferments/restructuring.

Credit and market risk emanating from investment portfolio is considered manageable.

Net investment portfolio represented around 52% (2019: 44%) of total asset base at end-Dec'2020. Investment in GoP instruments represented 91% of the total portfolio. Resultantly, Pacific at JP Morgan prior to joining HBL.

credit risk emanating from the investment portfolio is low. Total Pakistan Investment Bond (PIB) holdings were reported at Rs. 1.1tr (2020: Rs. 1.03tr, 2019: Rs. 623b) at end-1Q'21. Given the sharp decline in interest rates in 2020, the PIB portfolio recorded significant revaluation surplus. While a sharp reversal in interest rates is unlikely at this point in time, proactive market risk management is considered important in order to curtail potential mark to market losses on the PIB portfolio in case of any significant increase in interest rates.

While international operations incurred a sizeable loss, profitability is expected to improve going forward with China being the main focus area.

Overseas assets represent around one-tenth of total asset base. On international front, HBL remained focused on consolidation and de-risking along with strengthening governance and infrastructure through right sizing, developing client relationships, and enhancing network connectivity and technology capability. Pursuant to the same, HBL exited its business in Hong Kong. The Bank has also decided to exit its operations in Mauritius and is currently at an advanced stage of discussions with a potential buyer. The Afghanistan operations were ceased on June 10, 2019, with the remaining formalities for closure under progress. Going forward, China will be the key focus. HBL is one of only three banks across South Asia and MENA to offer end-to-end RMB intermediation. This capability, along with commencement of the Beijing branch operations is expected to strengthen relationships with Chinese clients, providing a competitive edge to the Bank versus regional and Pakistani Banks. Following the successful implementation of its China coverage model in the UAE, the Bank has extended this model to Bangladesh and Sri Lanka. Despite receding of New York related expenses, the international business reported a loss before tax of Rs. 13.6b (2019 Rs. 13.0b) on account of currency devaluation, an extensive de-risking exercise and higher credit provisions due to industry-wide credit issues in one of the international locations. Strategic focus of the international business segment will remain on leveraging of the China franchise, growing network business and strengthening trade, transaction banking and treasury capabilities.

Robust liquidity profile as evident from sizeable customer base along with cost effective & strong retail deposit mix. Significant liquidity buffers continue to support the liquidity profile of the Bank.

HBL caters to a sizeable and growing customer base of over 23 million customers. Moreover, an average of 0.92mn million new to bank (NTB) customers were added to the Bank's clientele annually during the past 4-years (2017-2020). The bank's deposit strategy will continue to focus on enhancing its deposit base through addition of NTB customers and deepening relationships with existing customers. The Ratings incorporate HBL's strong deposit mix, sizeable retail deposit base and manageable depositor concentration levels. While deposit concentration levels continue to increase on a timeline basis based on year-end deposits, deposit concentration level based on average deposit balances have remained within manageable levels. Besides improving deposit mix, overall liquidity profile is supported by sizeable liquid assets in relation to total deposits and borrowings. Liquidity Coverage Ratio and Net Stable Funding Ratio (NSFR) were reported at 245% (2020: 256%; 2019: 155%) and 170% (2020: 182%; 2019: 176.1%) respectively, at end-1Q'21 and are comfortably above the regulatory requirement of 100%.

Sound capitalization indicators

Overall capitalization indicators are sound with HBL's strong focus on maintaining and enhancing capital buffers as reflected by a conservative dividend payout policy, issuance of Additional Tier-1 (issued in 2019) capital and efforts to optimize risk weighted assets growth being a key rating driver. Given higher pace of growth in NPLs in comparison to equity, net NPL(s) in relation to Tier-1 capital (adjusted for General Provisioning) increased to 4.31% (2020: 4.35%, 2019: 3.75%) at end-Mar'21; however, the ratio remains compliant with the benchmarks for the assigned ratings.

In Dec'20, the bank exercised its call option on the outstanding Term Finance Certificates (TFCs eligible for recognition as Tier-II Capital) which stood fully redeemed on Feb 19, 2021. There is no capital implication of this redemption since the bank had excess Tier-II capital buffer which was not recognized in the CAR calculation. In fact, the recall supports the Bank's Tier I capital resulting from lower financial charges.

HBL's Tier-1 and overall CAR (unconsolidated basis) have improved on a timeline basis since 2017 and were reported at 15.2% (2020: 14.8%; 2019: 13.7%) and 19.7% (2020: 19.2%, 2019: 17.1%) at end-Mar'21, respectively. The improvement was supported by the SBP's relaxation in Capital Conservation Buffer (CCB) requirement by 100bps, as a result of which 42 bps of additional Tier II capital became eligible consequently strengthening the total CAR of the Bank. Tier-1 and overall CAR ratios of the bank stand well above regulatory requirements.

Profitability profile expected to improve over the rating horizon

Despite a steep decline in the benchmark rates, net interest income of the bank improved during 2020 driven by spread improvement, and volumetric growth in earning assets. Spreads improved on account of immediate repricing of liabilities vis-a vis assets. Management expects growth in markup income going forward to emanate from higher volume of loans and advances. Total non-markup income improved by ~37% during 2020 and amounted to Rs. 25.7b (2019: Rs. 18.8b). This was due to sizeable capital gains on federal government securities amounting to Rs. 8.2b in 2020. Since the costs related to New York and Business Transformation Program have subsided, the cost-income ratio of the bank improved to 59% (2019: 72%) during 2020.Going forward, the management has planned to bring down cost-income ratio to around 50%, driven by growth in recurring income from operations and bringing efficiencies to current operations. Going forward, projected increase in advances portfolio is expected to yield higher profits to the Bank. Moreover, normalization of expenses particularly with regards to international operations is expected to facilitate growth in profitability during 2021. Profitability indicators are expected to align with rating benchmarks over the rating horizon.

FINANCIAL SUMMARY *(amounts in PKR millions) – Annexure I*					
BALANCE SHEET	**2017**	**2018**	**2019**	**2020**	**1Q21**
Investments	1,335,791	1,341,031	1,351,962	1,912,238	1,686,134
Net Advances	800,689	1,015,854	1,073,019	1,117,321	1,102,014
Total Assets	2,573,950	2,879,495	3,053,734	3,643,712	3,344,942
Borrowings	395,486	518,896	382,072	540,095	280,614
Deposits & other accounts	1,899,511	2,020,008	2,301,899	2,669,491	2,630,211
Subordinated Loans	9,994	9,990	22,360	22,356	12,374
Tier-1 Equity	129,237	134,410	155,251	183,378	187,562
Paid Up Capital	14,669	14,669	14,669	14,669	14,669
Net Worth	172,639	179,049	201,422	242,725	240,023
INCOME STATEMENT					
Net Spread Earned	77,630	76,016	94,626	122,052	30,062
Net Provisioning / (Reversal)	88	4,640	2,530	10,224	1,727
Non-Markup Income	30,953	16,445	18,759	25,743	7,375
Administrative expenses	56,228	70,327	82,709	83,152	21,350
Profit/ (Loss) Before Tax	27,488	19,849	27,099	52,994	14,000
Profit / (Loss) After Tax	7,731	11,789	15,064	31,524	8,298
RATIO ANALYSIS					
Market Share (Domestic Advances)	10.8%	11.6%	11.6%	11.6%	NA
Market Share (Domestic Deposits)	14.3%	14.1%	14.6%	14.1%	NA
Gross Infection	7.76%	6.61%	6.34%	6.32%	6.36%
Provisioning Coverage	95%	93%	96%	101%	102%
Net Infection	0.78%	0.82%	0.55%	0.74%	0.77%
Cost of deposits	2.44%	3.13%	5.44%	4.49%	3.48%
Gross Advances to Deposits Ratio	44%	51%	47%	40%	40%
Net NPLs to Tier-1 Capital	5%	6%	4%	4%	4%
Capital Adequacy Ratio (CAR)	15.79%	16.38%	17.07%	19.20%	19.66%
Markup Spreads	3.29%	3.14%	3.53%	4.04%	3.72%
Efficiency	57%	78%	72%	59%	59%
ROAA	0.3%	0.4%	0.5%	0.9%	0.9%
ROAE	5.0%	7.5%	8.8%	16.4%	16.0%
Liquid Assets to Deposits & Borrowings	62%	64%	60%	65%	65%

** Annualized*

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 Entity	Habib Bank Limited
Sector	Commercial Banks
Type of Relationship	Solicited
Purpose of Rating	Entity & TFC Rating

Rating History

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
		RATING TYPE: ENTITY		
30-Jun-21	AAA	A-1+	Stable	Reaffirmed
30-Jun-20	AAA	A-1+	Stable	Reaffirmed
28-Jun-19	AAA	A-1+	Stable	Reaffirmed
31-Dec-18	AAA	A-1+	Stable	Maintained
29-June-18	AAA	A-1+	Negative	Reaffirmed
22-Sep-17	AAA	A-1+	Negative	Maintained
30-June-17	AAA	A-1+	Stable	Reaffirmed
30-June-16	AAA	A-1+	Stable	Reaffirmed
30-June-15	AAA	A-1+	Stable	Reaffirmed
30-June-14	AAA	A-1+	Stable	Reaffirmed
28-June-13	AAA	A-1+	Stable	Reaffirmed
26-June-12	AAA	A-1+	Stable	Upgrade
29-June-12	AA+	A-1+	Stable	Reaffirmed
13-June-11	AA+	A-1+	Stable	Reaffirmed
29-June-10	AA+	A-1+	Stable	Reaffirmed

Rating Date	Medium to Long Term	Rating Outlook	Rating Action
	RATING TYPE: TFC-1 (Tier-2)		
18-Jun-21			Matured
30-Jun-20	AAA	Stable	Reaffirmed
28-Jun-19	AAA	Stable	Reaffirmed
31-Dec-18	AAA	Stable	Maintained
29-June-18	AA+	Negative	Reaffirmed
22-Sep-17	AA+	Negative	Downgrade
30-Jun-17	AAA	Stable	Reaffirmed
30-Jun-16	AAA	Stable	Reaffirmed
17-Dec-15	AAA	Stable	Final
30-Jun-15	AAA	Stable	Preliminary

Rating Date	Medium to Long Term	Rating Outlook	Rating Action
	RATING TYPE: TFC-2 (ADT-1)		
30-Jun-21	AA+	Stable	Reaffirmed
30-Jun-20	AA+	Stable	Reaffirmed
28-Jun-19	AA+	Stable	Final
31-Dec-18	AA+	Stable	Preliminary

Instrument Structure (Tier 2)	In Dec'20, the bank exercised its call option on the outstanding Term Finance Certificate (TFCs eligible for recognition as Tier II Capital) which stood fully redeemed on Feb 19, 2021.

<table>
<tr><td>Instrument Structure (Tier 1)</td><td>Privately placed, perpetual, unsecured, subordinated, non-cumulative and contingent convertible Additional Tier-I (ADT-1) TFC amounting Rs. 12.4b.</td></tr>
<tr><td>Statement by the Rating Team</td><td>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.</td></tr>
<tr><td>Probability of Default</td><td>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.</td></tr>
<tr><td>Disclaimer</td><td>Information herein was obtained from sources believed to be accurate and reliable; however, VIS does not guarantee the accuracy, adequacy or completeness of any information and is not responsible for any errors or omissions or for the results obtained from the use of such information. For conducting this assignment, analyst did not deem necessary to contact external auditors or creditors given the unqualified nature of audited accounts and diversified creditor profile. Copyright 2021 VIS Credit Rating Company Limited. All rights reserved. Contents may be used by news media with credit to VIS.</td></tr>
<tr><td>Due Diligence Meetings Conducted</td><td>
<table>
<tr><th></th><th>Name</th><th>Designation</th><th>Date</th></tr>
<tr><td>1</td><td>Mr. Rayomond Kotwal</td><td>CFO</td><td>14-June-2021</td></tr>
<tr><td>2</td><td>Mr. Irfan Ahmed Meer</td><td>Financial Controller</td><td>14-June-2021</td></tr>
<tr><td>3</td><td>Mr. Nassir Salim</td><td>Head of Branch Banking</td><td>18-June-2021</td></tr>
<tr><td>4</td><td>Mr. Aamir Arshad</td><td>Head Corporate, Commercial & Investment Banking</td><td>18-June-2021</td></tr>
<tr><td>5</td><td>Mr. Tariq Masaud</td><td>Chief Risk Officer</td><td>18-June-2021</td></tr>
<tr><td></td><td></td><td></td><td></td></tr>
</table>
</td></tr>
</table>