RATING REPORT

Zarai Taraqiati Bank Limited

REPORT DATE:
June 30, 2022

RATING ANALYSTS:

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RATING DETAILS				
	Latest Rating		Previous Rating	
Rating Category	**Long-term**	**Short-term**	**Long-term**	**Short-term**
Entity	AAA	A-1+	AAA	A-1+
Outlook	Stable		Rating Watch-Developing	
Rating Date	*Jun 30,'22*		*Jun 30,'21*	

COMPANY INFORMATION	
Incorporated in 2002	**External Auditors:** BDO Ebrahim & Co Chartered Accountants
Public Limited Company	**Chairman of the Board:** Mr. Nadeem Lodhi*
Key Shareholders (with stake 5% or more)	**Chief Executive Officer:** Mr. Muhammad Shahbaz Jameel
State Bank of Pakistan: 76.23% Government of Pakistan: 23.75%	

APPLICABLE METHODOLOGY(IES)
VIS Entity Rating Criteria: Government Supported Entities (July 2020) **http://www.vis.com.pk/kc-meth.aspx**

*Mr. Nadeem Lodhi has tendered his resignation on March 09, 2022 which is under process for approval from Federal Government.

Zarai Taraqiati Bank Limited

OVERVIEW OF THE INSTITUTION

ZTBL, formerly Agricultural Development Bank of Pakistan (ADBP), was formed through the repeal of ADB Ordinance 1961. ADBP was established following the merger of Agricultural Development Finance Corporation and Agricultural Bank of Pakistan. ZTBL took over all assets, business, contracts, and liabilities of ADBP and started its countrywide operations as a public limited banking company on December 14, 2002. The bank has the mandate to provide finance and credit facilities to small farmers and low-income households.

Profile of Chairman

Mr. Nadeem Lodhi was appointed as Chairman of the Board in Dec'20 by Government of Pakistan. Mr. Lodhi has more than three decades of experience as emerging markets banker. He has served as Managing Director at ANZ Gindlays Bank P.I.C, Abraj Capital and DIB Capital Ltd. He also held positions of Citi Country Officer at Citi Bank, Uganda; Business & Governance Head at Citi Bank, Afghanistan; and as Citi Country Officer & Corporate Bank Head at Citi Bank, Pakistan).

Profile of CEO

ZTBL's management team is headed by Mr. Muhammad Shahbaz Jameel. Mr. Jameel has an extensive experience of over 28 years of working with different financial institutions. He has served at various positions including Acting Managing Director / Group Head at The Bank of Khyber and Pak Oman Investment Company and Regional Head-North at HBL.

RATING RATIONALE

The ratings assigned to Zarai Taraqiati Bank Limited (ZTBLincorporate the strong and continuing implicit support of the State Bank of Pakistan and Government of Pakistan (GoP) being the shareholders of the Bank. The ratings also incorporate the fundamental role of ZTBL in the overall ecosystem of the country since the Bank remains the principal development financial institution used as an agricultural financing arm by the GoP. The revision in ratings outlook take into account the withdrawal of the government guarantee on entire deposits of ZTBL available under Bank Nationalization Act 1974 (BNA), which has been replaced with Deposit Protection Scheme. However, the ratings factor in the socio-economic position of ZTBL as an important Rural Finance Institution and the continued support of its sponsors to deliver their targeted social objectives.

The gross loan portfolio of ZTBL has been depleting on a timeline basis on account of lower disbursements amidst portfolio consolidation. During FY21, the Bank reported profit before tax, after being in loss for the last four years, on the back of improvement in internal control measures leading to higher recoveries and lower incidence of fresh infection. While infection ratios have exhibited some improvement on a timeline basis, the Bank's asset quality remained compromised with limited loss absorption capacity as reflected by high net NPLs to Tier-1 equity. Meanwhile, liquidity has remained adequate with higher investments in government securities. Given considerable portion of PIBs are floating rate, market risk arising from the same is considered manageable. Capitalization has remained sound with CAR well above the regulatory requirement.

The Bank reported modest net profit in 1QFY22 on account of net reversals in provisioning in line with higher recoveries, as compared to sizeable provisioning charge in the preceding period last year. The management is projecting the bottom line to turn positive in the ongoing year on the back of higher recoveries and curtailment of non-performing loans as a result of digitization and strengthened internal control measures. Amount of loans rescheduled under the SBP Covid relief scheme as proportion of net advance portfolio was 2.4%, the same is expected to have controlled impact on asset quality over the rating horizon. Going forward, meeting recovery targets, improving asset quality indicators and maintaining liquidity and CAR at an adequate level will remain key rating sensitivities for the standalone strength and risk profile of the Bank.

Key Rating Drivers:

Advances: The bank largely met the disbursement target for the outgoing year. The Bank remained focussed towards increasing development loans during 2021. Resultantly, there was a slight change in loan portfolio mix as development loans proportion increased to 31% (FY20: 24%) of the total disbursements while the rest constituted production loans. Sada Bahar Scheme (SBS) remained the flagship product of the bank.

The bank rescheduled loans amounting Rs. 2.7b under the relief provided by SBP for Covid-19 during FY20, the closing amount of same facility stood at Rs 2.2b at end-FY21. GoP allocated markup subsidy amounting Rs. 6.8b for customers of ZTBL effective from July 22, 2020. Under this relief package, new and existing regular borrowers with landholdings up to 12.5 acres were eligible for markup subsidy at rate of 10% up till June 30, 2021. The borrowers availed Rs. 5b against this subsidy.

The portfolio concentration in Punjab remained largely the same during the outgoing year, which is in line with the highest population and agricultural related activity. The Board has formed 'Product Development and Marketing Committee' to develop new products to tap geographic potential and diversify loans. During FY21, the bank has launched four new development loan products. These include, financing for 'Establishment of Agri Tourist Outlet/Orchard', in Gilgit Baltistan; five green banking products under the 'Green Banking Guidelines of State Bank of Pakistan (SBP)' and 'Green Banking Policy of ZTBL'; financing scheme for 'Dairy Value Chain' for the dairy farming community and financing scheme for 'Agri Land Development through Alternate/Renewable Energy'. In addition, four products including financing for 'Farm Transport (three-wheeler loader rikshaw)', agri financing schemes for raw sugar (jaggery/shakkar making, packing and marketing), agri financing scheme for tea cultivation, packing and marketing and financing scheme for women empowerment entailing garments making has been launched in last quarter of the outgoing year. The above-mentioned products may require time to make significant inroads in the bank's portfolio. The maximum per borrower/party limit has been revised to Rs. 5m.

Asset Quality: Asset quality indicators of the Bank depicted improvement in the outgoing year on account of decline in NPLs to Rs. 40.8b (FY20: Rs. 59.2b). Therefore, despite modest growth in performing portfolio; gross loan portfolio of the Bank stood lower at Rs. 115.3b (FY20: Rs. 129.9b). Meanwhile, decrease in NPLs was on account of dual impact of recoveries and loans charged off during the outgoing year. During FY21, notable improvement in recoveries was made on account of multi-channel strategy adopted by the Bank. Gross and net infection ratios decreased to 35.4% (FY20: 45.6%) and 21.5% (FY20: 33.1%), respectively by end-FY21. Albeit absolute value of specific provisions held by the Bank decreased, provisioning coverage remained intact. As a matter of prudence, ZTBL has not availed the benefit of allowed value of mortgaged lands and buildings while computing the provision against nonperforming loans. As per management, infection ratios are expected to improve going forward on account of strengthened internal controls, resulting in prudent lending and transparency.

Investments: Net investments of the bank augmented to Rs. 82.4b (FY20: Rs. 39.8) by end-FY21; the increase was mainly manifested in T-bills which accounted for nearly half of the total portfolio. Overall exposure of Government securities increased to 94% (FY20: 85%). Credit risk emanating from investment portfolio is considered low. Given around two-third of the PIBs are floating rate, market risk arising from the same is considered low. Fixed rate PIBs accounted for one-third of the total PIBs investment in FY21; the bank recorded a deficit of Rs. 873.0m (FY20: Rs. 195.5m) arising from mark to market losses on government securities portfolio which largely pertained to five-year fixed rate PIBs. The equity portfolio comprises investment in a blue-chip stock, which carries sizeable unrealized surplus; the bank also receives regular dividend from the said investment. Investment portfolio of the bank decreased slightly by end-1QFY22; deficit on revaluation largely related to fixed rate PIBs amounted to Rs. 860.8m. Going forward, in line with conservative investment strategy, the bank plans to largely maintain the current investment mix.

Liquidity: The liquidity position of the bank is underpinned by sizeable coverage of deposits and borrowing via liquid assets (FY21: 54.9%; FY20: 44.9%). Total deposit base of the bank decreased to Rs. 43.6b (FY20: Rs. 49.2b) by end-FY21, as some high-cost deposits were offloaded to control funding cost. Proportion of CASA in total deposit mix remained at ~30%. Corporate deposits accounted for three-fourth of the deposit base while the rest pertained to retail deposits. Top 10 deposits constituted 66% (FY20: 63%) of the total deposit base; however, the concentration risk is considered manageable given 35% (FY20: 31%) of the deposits pertained to ZTBL Pension Fund. Around one-third of funding (excluding deposits) comprised redeemable preference shares issued to SBP carrying a fixed rate of 7.5% while the rest constituted repo borrowings, secured against market T-bills and PIBs. During the outgoing year, the Bank has devised a plan to counter the liquidity risk that may arise due to maturity gap in 5-year plus bucket owing to bullet repayment of SBP preference shares. The Bank's liquidity coverage ratio (LCR) and net stable funding ratio (NSFR) have remained comfortable on a timeline basis.

Profitability: Despite contraction in average advances portfolio, the Bank posted 24.8% growth in markup income during the outgoing year on the back of increase in markup earned on net advances and investments portfolio. Markup expensed, grew by 6.4% in FY21 owing to sizeable decrease in markup expense on deposits. Weighted average return on net advances portfolio increased to 20.95% (FY20: 16.46%) mainly on the back on regularization of some loans along with some increase in average markup rates during FY21. Markup income suspended on NPLs decreased considerably to Rs. 10.4b (FY20: Rs. 15.3b). Overall yield on markup bearing assets decreased marginally, whereas cost of funds decreased by ~129 bps. Resultantly, markup spread increased by ~118 bps. Efficiency ratio of the Bank has improved notably amidst higher total income and lower operating expenses. Net provision and write-offs reduced to Rs. 777.7m (FY20: Rs. 1.3b). ZTBL posted Rs. 1.8b in profit before tax vis-à-vis loss before taxation of Rs. 3.2b in the preceding year. However, the Bank reported net losses on account of significantly higher tax charge of Rs. 3.5b (FY20: Rs. (757.1m). As the bank reported profit before tax, the net provisioning is allowed only upto 1% of GLP, which led to incremental tax charge during FY21.

Capitalization: Tier-1 capital (CET-1) of the Bank decreased from Rs. 46.9b in FY20 to Rs. 45.0b in FY21 on account of increase in accumulated losses. As a result of reduction in NPLs, net NPLs in relation to Tier-I equity (adjusted for general provisioning) decreased by end-FY21 and 1QFY22, albeit, remained on a much higher side relative to the benchmarks for the assigned ratings. Total CAR of the Bank has remained well above the regulatory requirement. Despite decrease in total eligible capital, slight improvement in CAR at end-FY21 and 1QFY22 is on account of decrease in Risk Weighted Assets (RWA) largely due to lower credit risk assets amidst improvement in portfolio quality.

Digitization: Over the last three years, the Bank has improved internal control systems through digitization. This majorly encompasses digitization of Credit Administration Department (CAD), centralization of loan approval system, creation of Central Loan Sanctioning Department (CLSD) at HO under the administration of Enterprise Risk Management Division (ERMD). At present, the Bank is under process of centralizing Credit Administration (CA) function from HUBs to head office for better control and monitoring. In addition, the Bank has deployed various information system tools in compliance and risk divisions. The Field Vehicle Tracking System has been installed while MCO Movement Tracking System is under testing phase and expected to be launched soon. Deployment of Managed Network Infrastructure is in progress and the footprint has reached 44 branches as on Dec 31, 2021. Biometric verification of regular borrowers, classified borrowers and normal priority active depository accounts have been 99%, 91% and 99.8%, respectively while the Bank has completed the biometric verification of high and medium priority depository accounts. Meanwhile, acquisition of core banking system has suffered delays. The Bank has hired external specialist to gather specific requirements.

Corporate Governance: Bank (Nationalization) Act, 1974 states that the Chairman, the President, and other members of the Board, representing Federal Government's direct and indirect shareholding, shall be appointed by the Federal Government in consultation with the State Bank of Pakistan (SBP), for a term of three years, on such terms and conditions as may be fixed by the General Meeting of the Bank. Further the Bank has setup a Nomination Committee as per Public Sector Companies (Corporate Governance) Rules, 2013 to identify, evaluate and recommend candidates for vacant positions. Presently, the Board comprised seven members, including Chairman, president, two independent directors and three non-executive directors.

Due to non-functional Board in previous years, SBP imposed restrictions on new hiring or appointments which have not been lifted yet. Owing to these restrictions, the bank is facing various issues which have been impacting the Bank's performance at multiple levels. One of them is that around 31% of the Bank employees are in the age bracket of 55 to 60 years and significant number of employees above the rank of OG-1 have been leaving the organization under retirement, exit policy, deceased, resignations etc. for the past few years. The bank is also facing acute shortage of field functionaries. The bank also plans to separate operations from banking business activities and replenish the retiring/leaving officers/executives with market based professional bankers that has been hampered due to hiring restrictions. Meanwhile, according to the management, no critical position is currently vacant as the identified successors were promoted to relevant positions. The Financial Statements for FY21 were audited by BDO Ebrahim & Co Chartered Accountants, who have been reappointed for FY22.

Zarai Taraqiati Bank Limited — Annexure I

FINANCIAL SUMMARY			*(Amounts in PKR billions)*	
BALANCE SHEET	**31-Dec-19**	**31-Dec-20**	**31-Dec-21**	**31-Mar-22**
Total Investments	24.1	39.8	82.4	80.9
Gross Advances	140.2	129.9	115.3	107.9
Total Assets	**199.9**	**210.7**	**254.8**	**241.1**
Borrowings	72.5	81.2	132.3	130.5
Deposits & other accounts	46.0	49.2	43.6	32.2
Paid-Up Capital	52.7	52.7	52.7	52.7
Tier-1 Equity	48.0	46.9	45.0	45.1
Net Worth	57.6	56.7	53.9	54.1
INCOME STATEMENT	**31-Dec-19**	**31-Dec-20**	**31-Dec-21**	**31-Mar-22**
Net Mark-up Income	8.6	8.3	12.2	3.1
Net Provisioning/ (reversal)	25.3	1.3	0.8	(0.4)
Non-Markup Income	1.8	1.3	1.3	0.3
Operating Expenses	12.7	11.5	10.9	3.0
Profit/(Loss) Before Tax	-26.3	-3.2	1.8	0.8
Profit/(Loss) After Tax	-17.6	-2.5	-1.7	0.2
RATIO ANALYSIS	**31-Dec-19**	**31-Dec-20**	**31-Dec-21**	**31-Mar-22**
Advances to Deposit Ratio (%)	305%	264%	264%	335%
Liquid Assets to Deposits & Borrowings (%)	41%	44%	54%	50%
NPLs	60,278	59,225	40,800	31,557
Gross Infection (%)	43.0%	45.6%	35.4%	29.2%
Provisioning Coverage (total) (%)	50.5%	46.0%	57.5%	57.9%
Net Infection (%)	29.1%	33.1%	21.5%	17.6%
Cost of Funds (%)	8.73%	8.43%	7.14%	8.68%
Net NPLs to Tier-1 Capital (%)	59.1%	63.7%	42.3%	33.8%
Tier-1 Capital Adequacy Ratio (CAR (%))	27.8%	28.3%	30.7%	32.0%
Total CAR (%)	30.0%	30.4%	32.7%	33.7%
LCR (%)	618%	784%	728%	725%
NSFR (%)	128%	128%	127%	127%
Markup Spreads (%)	4.99%	4.89%	6.06%	5.43%
Efficiency (%)	124%	121%	81%	89%
ROAA (%)	n.m.	n.m.	n.m.	0.3%
ROAE (%)	n.m.	n.m.	n.m.	1.3%

ISSUE/ISSUER RATING SCALE & DEFINITIONS — Annexure 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	**Annexure III**
Name of Rated Entity	Zarai Taraqiati Bank Limited (ZTBL)
Sector	Specialized Bank
Type of Relationship	Solicited
Purpose of Rating	Entity Ratings
Rating History	

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
RATING TYPE: ENTITY				
30-June-22	AAA	A-1+	Stable	Maintained
30-June-21	AAA	A-1+	Rating Watch-Developing	Maintained
30-June-20	AAA	A-1+	Stable	Reaffirmed
26-June-19	AAA	A-1+	Stable	Reaffirmed
28-June-18	AAA	A-1+	Stable	Reaffirmed
20-June-17	AAA	A-1+	Stable	Reaffirmed
16-June-16	AAA	A-1+	Stable	Reaffirmed
18-June-15	AAA	A-1+	Stable	Reaffirmed
08-August-14	AAA	A-1+	Stable	Upgrade

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	

Name	Designation	Date
Mr. Muhammad Arif	CFO	6th June'22
Mr. Arshad Hassan Awan	Head Credit Division	6th June'22
Mr. Salman Arshad	Head Enterprise Risk Management Division	6th June'22
Rana Mujahid Ali Khan	Head Recovery & SAM Division	6th June'22
Mr. Waqas Ahmad	Head Internal audit & Inspection Division	6th June'22
Mr. Amir Zafar	Group Head IS Division, Digital Banking Division & Service Division.	6th June'22