RATING REPORT

Meezan Bank Limited (MBL)

REPORT DATE:
June 30, 2020

RATING ANALYSTS:
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RATING DETAILS

Rating Category	Latest Rating		Previous Rating	
	Long-term	**Short-term**	**Long-term**	**Short-term**
Entity	AA+	A-1+	AA+	A-1+
Sukuk (Tier-2)	AA		AA	
Sukuk (Tier-1)	AA-		AA-	
Rating Outlook	Stable		Stable	
Rating Date	*June 30th '20*		*June 28th'19*	

COMPANY INFORMATION

Incorporated in 1997	External auditors: **M/S EY Ford Rhodes**
Public Limited Company	Chairman of the Board: **Mr. Riyadh S.A.A. Edrees**
Key Shareholders* (with stake 5% or more):	Chief Executive Officer: **Mr. Irfan Siddiqui**
Noor Financial Investment Co, Kuwait – 35.25%	
Pakistan Kuwait Investment Co. (Pvt.) Ltd. – 30.00%	
Islamic Development Bank, Jeddah – 9.32%	
***as of the report date**	

APPLICABLE METHODOLOGY(IES)

Rating Methodology Commercial Banks (March 2018):
http://vis.com.pk/kc-meth.aspx

OVERVIEW OF THE INSTITUTION	RATING RATIONALE
Meezan Bank Limited is the largest Islamic commercial bank in Pakistan, which commenced operations in March'2002, after being issued the first ever Islamic commercial banking license by the State Bank of Pakistan (SBP)	Meezan Bank Limited (MBL) is the first and largest Islamic commercial bank of the country. Over the last decade, MBL has significantly expanded its operations; presently, MBL's distribution network is spread across 774branches, operating in more than 220cities/towns across Pakistan. Consequently, MBL is currently positioned as the seventh largest bank in Pakistan. MBL has been rated at 'AA+/A-1+', which is indicative of high credit quality and strong protection factors, with slight sensitivity to changing economic conditions. As per our review, MBL's asset quality, liquidity and capitalization metrics remain within the thresholds for the assigned ratings. Furthermore, the profitability metrics have improved and remain comparable to peers.
Noor Financial Investment Company Limited, Pakistan Kuwait Investment Company (Pvt.) Limited and Islamic Development Bank are the primary shareholders of MBL	Major shareholding of MBL rests with Noor Financial Investment Company (NFIC) (35.25%), Pakistan Kuwait Investment Company (Pvt.) Ltd (PKICL) (30.00%) and Islamic Development Bank, Jeddah (IDB) (9.32%). **Market position has been maintained.** At end-2019, MBL had market share of 6.2% in terms of gross advances and 6.4% in terms of deposits. MBL's continued asset growth arose from the strong performance in both the retail and corporate deposit market. MBL's ADR, at 54.3% (2018: 66.5%), stands above the median ADR of peer 'AA+' rated banks. At the same time, MBL's liquid asset to funding ratio stands lower than the peer median.
Profile of Chairman Mr. Riyadh Edrees serves as Chairman of the Board. Mr. Edrees holds more than 25years of experience at various organizations	**MBL pursued deliberate strategy of portfolio consolidation instead of growth in view of economic situation. Focus will remain on cautious lending amid ongoing COVID-19 situation and ensuing economic slowdown.**
Profile of CEO Mr. IrfanSiddiqui is the founding President and CEO of MBL Mr. Siddiqui is a qualified Chartered Accountant from the Institute of Chartered Accountants of England & Wales.	Recognizing the increased risk factors that emanate from the overall slowdown in the economy, MBL slowed the growth of its Islamic financing portfolio in 2019. The portfolio continues to be dominated by corporate clientele, which comprises about two-thirds of the financing exposures. MBL may pursue selective growth in CBSME and Consumer segments, which are relatively high/medium risk/return segments. Government's decision to enhance limits of SME borrowers in the wake of COVID-19 pandemic provides additional incentive to MBL to cater to this segment. Sector concentration in power, oil& gas, textile and food & agriculture persists. Gross advances decreased to Rs. 487b by end-1Q20. **Assets quality indicators compare favorably to peers. In the long run, asset quality indicators may be impacted by negative impact of COVID-19 on repayment capacity of borrowers.** Despite a rising credit risk environment– MBL has been able to maintain its asset quality. As of Dec'19, MBL's gross infection stood slightly higher at 1.8% (2018: 1.3%), comfortably below the peer group median. MBL maintains a comfortable level of provisions against its non-performing financings with a coverage ratio of 142% in December 2019 - one of the highest in the Banking industry. However, given the strong focus on corporate clientele, the portfolio does depict counterparty concentration, which although has decreased in December 19 vis a vis December 18. Some comfort can be derived from fact that exposures comprise of government guaranteed and blue-chip corporate clientele. Recent economic slowdown due to COVID-19 is expected to negatively impact repayment

capacity of borrowers for the Banking Industry in Pakistan as a whole; hence, asset quality indicators may witness pressure in the long run. In 2020, no impact will be observed on NPLs as SBP has allowed banks to defer clients' payment of principal on loan obligations by one year and also relaxed regulatory criteria for restructured/rescheduled loans for borrowers who require relief beyond the extension of principal repayment for one year. Maintaining assets quality indicators in line with rating benchmarks is considered an important rating driver going forward.

MBL's liquidity profile is strong and draws support from its strong ability to attract and retain deposit base.

MBL's liquidity profile is strong, given its strong ability to attract and retain deposit, as evident from the successive improvement in domestic deposit market share. Liquidity profile is further supported by the strong retail contribution, relatively higher tilt towards Current & Saving Accounts (CASA) and granularity of the deposits, which compares favorably to peers. For the year ended December 31, 2018 and 2019 individual customer deposits account to total deposits is 66.4% and 67.4% respectively, the highest percentage of individual customer deposits among all bank in Pakistan.

Increasing interest rates and higher non-markup income contributed to healthy growth in profitability and Equity (through internal capital generation) during the period under review; however, profitability is expected to come under pressure in medium to long term in view of decreasing interest rate scenario and client repayment capacity being affected due to economic slowdown.

Liquidity management remains a key challenge for Islamic Banking Industry of Pakistan as there are limited investment avenues despite sufficient liquidity. This puts MBL at a disadvantage in comparison to its peers, however, MBL profitability metrics trend in line with peers. The recent issue of Pakistan Energy Sukuk (PES)– I in 2019 and PES II along with GOP Ijarah Sukuk in first half of 2020 has partially addressed liquidity deployment challenge.

In the outgoing year, MBL's net profit increased by 70% to Rs. 15.2b (2018: Rs. 9.0b). The strong growth in the Bank's profitability enabled the Bank to further strengthen its capital base with CET 1 increasing by Rs. 9 billion – a 23% increase from last year. The Bank's CAR is at comfortable level of 16.58% in 2019. The growth in profitability is attributable to the volumetric growth in investments, along with increase in spread and growth in fee & commission based income mainly emanating from the growing trade finance business and higher forex income. Despite the increase in expense base, MBL was able to reduce the efficiency ratio, which stood comfortably below the 'AA+' rated banks.

Going forward, the COVID-19 crisis and its impact on the economy and the financial sector would make the operating dynamics of the banks in general challenging. SBP has announced regulatory relaxations to manage the asset quality of the banks' portfolio which along with the relief package provided by the Federal Government is expected to provide certain respite to the banks in the short term. Profitability of MBL will be further supported during 2020 on account of lag in re-pricing of loan portfolio and low cost of deposits with significant CASA tilt. However, the impact of curtailment of economic activity due to COVID-19 and lower lending rate scenario may cause margin compression, thereby impacting the profitability of MBL in the medium to long term. Moreover, impairment charges due to adverse impact of economic slowdown on client's repayment capacity may further exert downward pressure on profitability. Maintaining conservative lending strategy to maintain asset quality and cost efficiencies would be important rating drivers going forward.

Capitalization levels remain comfortably above the regulatory requirement and our criteria for 'AA+' rated banks. Capital buffers are considered adequate for the medium-term horizon.

Equity (excluding revaluation surplus) depicted increase on timeline basis due to internal capital generation. At Dec-end-2019, CAR of MBL remains comfortably at 16.58% - above the mandated regulatory requirement of 12.5%. In January 2020, the Bank successfully issued second tranche of Sub-ordinated Tier II Sukuk of Rs 4 billion in the form of regulatory compliant unsecured, sub-ordinated privately placed Sukuk that has further strengthened the Bank's Capital Adequacy Ratio. In order to encourage banks to extend further credit to customers to facilitate economic recovery, the SBP in March 2020 has reduced overall CAR requirement of by 1% to 11.5% from 12.5% till further instructions. CAR of MBL is expected to remain comfortable at 17.00%. MBL also has sufficient cushion to meet any adverse movement in credit, market and operational risks.

Meezan Bank Limited **Appendix I**

FINANCIAL SUMMARY (Rs. in billions)			
BALANCE SHEET	31-Dec-17	31-Dec-18	31-Dec-19
Total Investments	119.2	123.7	225.6
Gross Advances	428.8	522.2	506.5
Total Assets	788.8	937.9	1,121.3
Borrowings	36.8	36.4	42.0
Deposits & other accounts	667.2	785.5	932.6
Subordinated Sukuk (Tier II)	7.0	7.0	7.0
Subordinated Sukuk (Tier I)	-	7.0	7.0
Paid up Capital			
Tier-1 Equity	33.6	46.6	55.8
Net Worth	35.0	40.3	59.0
INCOME STATEMENT	31-Dec-17	31-Dec-18	31-Dec-19
Net Mark-up Income	20.8	28.1	46.5
Net Provisioning charge	1.3	1.1	4.2
Non-Markup Income	7.6	7.4	9.3
Administrative Expenses	16.6	19.2	24.8
Profit Before Tax	10.2	14.7	26.2
Profit After Tax	6.3	8.9	15.2
RATIO ANALYSIS	31-Dec-17	31-Dec-18	31-Dec-19
Market Share (Advances) (%)	6.60%	6.60%	6.21%
Market Share (Deposits) (%)	5.40%	5.90%	6.37%
Advances to Deposits Ratio (%)	64.3%	66.5%	54.3%
Liquid assets to Deposits and Borrowings (%)	43.8%	43.0%	54.5%
NPLs	6.6	7.0	9.0
Gross Infection (%)	1.50%	1.30%	1.78%
Provisioning Coverage (%)	133.3%	138.9%	141.6%
Net Infection (%)	0.04%	0.04%	0.14%
Cost of deposits (%)	2.30%	2.48%	5.04%
Net NPLs to Tier-1 Capital (%)	0.50%	0.46%	1.27%
Tier-1 CAR (%)	9.94%	12.00%	12.92%
Capital Adequacy Ratio (C.A.R) (%)	12.89%	14.55%	16.58%
LCR (%)	126.0%	147.0%	192.0%
NSFR (%)	132.0%	130.0%	163.0%
Markup Spreads (%)	3.93%	4.41%	6.32%
Efficiency (%)	60.70%	54.60%	44.55%
ROAA (%)	0.87%	1.04%	1.48%
ROAE (%)	19.26%	23.77%	30.66%
Fund Flow from Operations	n/a	n/a	n/a
Debt to Equity Ratio	n/a	n/a	n/a
Current Ratio	n/a	n/a	n/a

n/a: not applicable on banks

ISSUE/ISSUER RATING SCALE & DEFINITIONS Appendix II

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	Meezan Bank Limited
Sector	Commercial Banks
Type of Relationship	Solicited
Purpose of Rating	Entity and Sukuk Rating

Rating History

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
		RATING TYPE: ENTITY		
6/30/2020	AA+	A-1+	Stable	Reaffirmed
6/28/2019	AA+	A-1+	Stable	Reaffirmed
5/30/2018	AA+	A-1+	Stable	Upgrade
6/22/2017	AA	A-1+	Stable	Reaffirmed
6/2/2016	AA	A-1+	Stable	Reaffirmed
6/29/2015	AA	A-1+	Stable	Reaffirmed
6/24/2014	AA	A-1+	Stable	Reaffirmed
6/26/2013	AA	A-1+	Stable	Upgrade
6/1/2012	AA-	A-1+	Stable	Reaffirmed
6/1/2011	AA-	A-1+	Stable	Maintained

Rating Date	Medium to Long Term	Rating Outlook	Rating Action
	RATING TYPE: SUKUK-1		
6/30/20	AA	Stable	Reaffirmed
6/28/19	AA	Stable	Reaffirmed
5/30/18	AA	Stable	Upgrade
6/22/17	AA-	Stable	Reaffirmed
8/31/16	AA-	Stable	Preliminary
6/29/16	AA-	Stable	Preliminary

Rating Date	Medium to Long Term	Rating Outlook	Rating Action
	RATING TYPE: SUKUK-2		
6/30/20	AA-	Stable	Reaffirmed
6/28/19	AA-	Stable	Reaffirmed
8/20/18	AA-	Stable	Final
6/5/18	AA-	Stable	Preliminary

Instrument Structure	Basel III compliant Tier 2, privately placed, unsecured & subordinated Sukuk amounting to Rs. 7.0b and has a tenor of 10 years.
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.
Due Diligence Meetings Conducted With	**Mr. Shabbir Hamza Khandwala – Chief Financial Officer** **Mr. Abdullah Ahmed – Group Head of Corporate & Institutional Banking** **Mr. Syed Tariq Hassan – Chief Risk Officer**
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.
Disclaimer	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. VIS is