RATING REPORT

Sindh Bank Limited

REPORT DATE:
June 27, 2023

RATING ANALYST:
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RATING DETAILS

Rating Category	Latest Rating		Previous Rating	
	Long-term	**Short-term**	**Long-term**	**Short-term**
Entity	A+	A-1	A+	A-1
Outlook	Stable		Stable	
Action	*Reaffirmed*		*Reaffirmed*	
Date	*June 27, 2023*		*June 28, 2022*	

COMPANY INFORMATION

Incorporated in 2010	External auditors: **RSM Avais Hyder Liaquat Nauman Chartered Accountants**
Public Unlisted Company	Chairman of the Board: **Mr. Anis A. Khan**
Key Shareholders (with stake 5% or more):	Chief Executive Officer: **Mr. Imran Samad**
Government of Sindh, Finance Department – 99.9%	

APPLICABLE METHODOLOGY(IES)

VIS Financial Institution (June 2023)
https://docs.vis.com.pk/docs/FinancialInstitution.pdf

VIS Rating Scale
https://docs.vis.com.pk/docs/VISRatingScales.pdf

Sindh Bank Limited (SNDB)

OVERVIEW OF THE INSTITUTION

Sindh Bank Limited was incorporated as a public limited unlisted company in October 2010. Government of Sindh has 99.9% shareholding in the bank. The bank was operating with a network of 330 branches at end-2022

RATING RATIONALE

Headquartered in Karachi, Sindh Bank Limited (SNDB) is a wholly owned entity of Government of Sindh (GoS) with operating history of over a decade. The branch network stood at previous year level with total 330 branches (14 dedicated for Islamic banking) in 169 cities nationwide.

Banking Sector

The economy is currently facing several challenges, including a decrease in foreign reserves, a devaluing currency, and high inflation levels. To combat rising inflation, caused by the commodity super cycle and effects of Ukraine war, the central bank has implemented stricter monetary policies, resulting in a significant increase in the policy rate. This has led to higher funding costs for banks and impacted borrowers' debt servicing ability. As a result, banks are adjusting by increasing provisions for potential loan losses and writing off non-performing loans. The economic slowdown will likely prompt stricter lending standards with banks continuing to remain heavily invested in sovereign exposures. Counterbalancing this, rising interest rates should help banks widen their margins, partially offsetting the decline in earnings due to lower business volumes (financings and trade business) and still allowing for improved profitability. However, there is increased credit risk and market risk vulnerability, especially in the face of any potential interest rate or currency fluctuations, which could impact the capitalization levels of banks. Looking ahead, the medium to long-term outlook for the fiscal account is challenging because the government is struggling to expand its revenue base. Public debt accumulation is accelerating, crowding out private sector credit. This trend also increases the risk of potential sovereign debt restructuring. Given that banking sector balance sheets are highly skewed towards Government paper, this could lead to liquidity and profitability challenges, particularly for small and medium-sized banks in the future.

Key Rating Drivers

Credit portfolio indicators compare adversely to peers, with some improvement in its provisioning coverage.

Due to regulatory restriction on corporate lending, gross advances portfolio of SNDB has registered a declining trend on a timeline basis. Owing to same, market share (in terms of gross advances) has also declined from 0.72% as of Dec'21 to 0.59% as of Mar'23. Corporate loan book remains the highest proportion of the Bank's lending operations while overall client and sectoral concentration remains on the higher side. The management has reported that the Bank has seriously taken up consumer financing activity through its branch network as well as SME portfolio as a major step to diversify its credit portfolio with risk mitigating mechanism intact.

Non-Performing Loans (NPLs) demonstrate a decreasing trend, due to successful management and recovery of non-performing assets. Despite this, the gross infection ratio remains relatively high when compared to 'Small Banks'. The Bank has strengthened its provisions, as evident from the increasing specific and total provisioning coverage ratios.

The investment portfolio presents minimal credit, and relatively low market risk; liquidity ratios remain above regulatory requirements.

The investment portfolio is considered to have minimal credit risk exposure in the domestic context, being mostly held in government securities. Pakistan Investment Bonds (PIBs) comprise 97.0% (further bifurcated into 86% in Floating rate PIBs and 11% in fixed rate PIBs) of the total investments as of Mar'23. The market risk exposure is also manageable, especially when viewed in the context of the sector at large, with the holdings of legacy fixed-rate PIBs, available for sale, only constituting 6.1% (Dec'21: 9.3%) of the total investment portfolio. The Bank carries Mark-to-Market (MTM) losses amounting to Rs. 3.9b on its investments due to an increase in benchmark rates as at Mar'23. However, as per the Bank, the number is comparatively much lower than average mark to market losses of the industry.

As of Mar'23, SNDB experienced deposit base growth slower than the industry's deposit growth rate. As a result, the Bank's market share decreased slightly from 1.04% in Dec'21 to 0.95% in Mar'23. As of Dec'22, more than 2/3rd of the deposit base has been placed by the Government (Federal and Provincial). In terms of concentration, a gradual decrease in the top 5, top 20, and top 50 depositors is observed over the analyzed period.

SNDB's Liquidity Coverage Ratio (LCR) and Net Stable Funding Ratio (NSFR) experienced significant fluctuations but remained above the regulatory requirement, indicating a moderate liquidity risk profile.

SBP's monetary tightening led to elevated benchmark rates, impacting spreads, efficiency ratio, and income growth.

Due to the monetary tightening measures implemented by the State Bank of Pakistan (SBP) in 2022, the benchmark interest rates remained elevated throughout the year. On average, the benchmark rates in 2022 were around 550 basis points higher compared to 2021. Consequently, SNDB experienced a rise of approximately 420 basis points in the yield on its earning assets, while the cost of funding increased by roughly 440 basis points. As a result, a decrease in the Bank's spreads was observed throughout 2022, and remains relatively low compared to its peers. Net markup income still registered slight growth, mainly driven by growth in average balance in the investments portfolio.

The Bank's non-markup income experienced significant increase during the same period. This rise was due to higher foreign exchange and dividend income which was partially offset by realized loss on securities. Efficiency ratio has improved on a timeline mainly on account of growth in revenue and despite higher operating expenses. However, it still remains relatively weak compared to peer banks. Loss before provisions and taxes (LBPT) in 2022 was higher at Rs. 330m, with the profitability profile further affected by provisioning charges of Rs. 1.9b, translating into significant loss, despite a significant decrease in provision from Rs. 5.8b in 2021.

Capitalization indicators remain under pressure given weak internal capital generation. Sponsor support is required to meet capital requirement.

As of Mar'23, SNDB's Capital Adequacy Ratio (CAR) has experienced a substantial decline and was below the regulatory requirement. The management has stated that the Government of Sindh has approved the capital infusion of Rs. 5b by Jun'23, which will raise the CAR to 12.55%.

Capitalization indicators are expected to remain stressed throughout the rating timeframe due to limited internal generation of capital and the need for continued provisions against non-performing loans. At present, the ratio of net non-performing loans (NPLs) to Tier-1 equity is the highest in the industry.

Sindh Bank Limited **Appendix I**

FINANCIAL SUMMARY *(amounts in PKR millions)*			
BALANCE SHEET	**Dec'21**	**Dec'22**	**Mar'23**
Investments	175,703	254,553	248,260
Net Advances	47,784	43,802	42,803
Total Assets	270,188	357,850	372,874
Borrowings	26,786	106,935	119,759
Deposits & other accounts	217,608	223,044	223,052
Tier-1 Equity	5,689	2,296	73
Paid-up Capital	25,524	29,524	29,524
Shareholder's Equity	19,748	18,359	18,528
INCOME STATEMENT	**2021**	**2022**	**Q1'2023**
Net Markup income	4,904	5,316	1,543
Net Provisioning charge	(5,823)	(1,939)	154
Non-Markup Income	576	1,089	407
Administrative expenses	5,654	6,726	1,771
Profit/ (Loss) Before Tax	(6,064)	(2,269)	278
Profit / (Loss) After Tax	(3,727)	(1,385)	170
RATIO ANALYSIS	**Dec'21**	**Dec'22**	**Mar'23**
Market Share (Domestic Advances) (%)	0.72%	0.60%	0.59%
Market Share (Domestic Deposits) (%)	1.04%	0.99%	0.95%
Advances to Deposits Ratio (%)	32.8%	30.9%	30.5%
Liquid Assets to Deposits & Borrowings (%)	80.2%	82.0%	82.2%
NPLs	37,404	34,967	34,723
Gross Infection (%)	51.2%	49.3%	49.8%
Provisioning Coverage (%) *(incl. general provisions)*	67.5%	77.5%	77.6%
Net Infection (%)	25.5%	18.0%	18.2%
Cost of deposits (%)	5.11%	8.20%	11.80%
Net NPLs to Tier-1 Capital (%)	213.8%	343.1%	9273.6%
Tier-1 CAR (%)	11.9%	5.36%	0.15%
Capital Adequacy Ratio (CAR) (%)	11.9%	5.36%	0.15%
LCR (%)	441%	352%	435%
NSFR (%)	256%	203%	234%
Markup Spreads (%)	1.50%	1.29%	1.49%
Efficiency (%)	103.1%	102.6%	91.0%
ROAA (%)	(1.4%)	(0.4%)	0.7%*
ROAE (%)	(19.0%)	(7.3%)	14.7%*

**Annualized*

REGULATORY DISCLOSURES						Appendix II
Name of Rated Entity	Sindh 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					
	6/27/2023	A+	A-1	Stable	Re-affirmed	
	6/28/2022	A+	A-1	Stable	Re-affirmed	
	6/30/2021	A+	A-1	Stable	Re-affirmed	
	6/30/2020	A+	A-1	Stable	Re-affirmed	
	6/28/2019	A+	A-1	Stable	Downgrade	
	6/28/2018	AA	A-1+	Rating Watch-Developing	Re-affirmed	
	6/30/2017	AA	A-1+	Rating Watch-Developing	Maintained	
	6/28/2016	AA	A-1+	Stable	Re-affirmed	
	6/30/2015	AA	A-1+	Stable	Re-affirmed	
	12/23/2014	AA	A-1+	Stable	Upgrade	
	6/30/2014	AA-	A-1+	Positive	Maintained	
	6/28/2013	AA-	A-1+	Stable	Maintained	
	5/21/2012	AA-	A-1	Stable	Reaffirmed	
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.					
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Due Diligence Meeting Conducted	**Name**	**Designation**	**Date**			
	Mr. Muhammad Anwaar	Chief Operating Officer	**25-May-2023**			
	Mrs. Rukhsana Narejo	Head of Treasury				
	Mrs. Ruqaya Marghoob	Head of Corporate				
	Mr. Dilshad Hussain Khan	Chief Financial Officer				