RATING REPORT

Bank Alfalah Limited

REPORT DATE:
July 15, 2019

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+
Rating Outlook	Stable		Stable	
Rating Date	*2nd July, '19*		*29th June, '18*	
TFC (Tier-1)	AA-		AA-	
Rating Outlook	Stable		Stable	
Rating Date	*2nd July, '19*		*29th June, '18*	

COMPANY INFORMATION

Incorporated in 1992	**External auditors:** **2017:** KPMG Taseer Hadi & Co. Chartered Accountants **2018:** EY Ford Rhodes & Co. Chartered Accountants
Public Limited & Listed Company	**Chairman of the Board:** H.H. Sheikh Nahayan Mabarak Al Nahayan
Key Shareholders (with stake 5% or more):	**Chief Executive Officer:** Mr. Nauman Ansari
H.H. Sheikh Nahayan Mabarak Al Nahayan, Chairman – 10.68%	
H.H. Sheikh Hamdan Bin Mubarak Al Nahayan – 8.39%	
H.E. Sheikh Suroor Bin Mohammad Al Nahyan – 7.13%	
M/S. Electro Mechanical Company LLC – 5.45%	
M/S. International Finance Corporation – 14.76%	
***As at Dec'18**	

APPLICABLE METHODOLOGY

VIS Commercial Banks Rating – March 2018
http://jcrvis.com.pk/docs/Meth-CommercialBanks201803.pdf

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Bank Alfalah Limited

OVERVIEW OF THE INSTITUTION

Bank Alfalah Limited (BAFL) was established as a privately held bank in 1992. Currently the bank operates as a public limited company with majority shareholding held by Abu Dhabi Group.

Profile of CEO

Mr. Nauman Ansari served various banks during his over 24-year professional career, including leading institutions like Standard Chartered Bank, Bank of America, ABN Amro, Fortis Bank and Samba. He is a business graduate of Miami University, USA.

Profile of Chairman

His Highness Sheikh Nahayan Mabarak Al Nahayan is a prominent member of the ruling family of Abu Dhabi, United Arab Emirates. Currently, His Highness is UAE Cabinet Member and also minister of State for Tolerance. Prior to his current responsibility, he also served as Minister of Culture and Knowledge Development; Minister of Culture, Youth, and Social Development, and Minister of Higher Education and Scientific Research.

RATING RATIONALE

Strong sponsors, diversified operations and established franchise.

Ranked eighth largest in the commercial banking sector, in terms of domestic deposits, Bank Alfalah Limited ('BAFL' or 'the bank') is sponsored by the Abu Dhabi Group (ADG), comprising some of the prominent members of UAE's ruling family and leading businessmen. Over the years, the bank has developed a strong franchise recall, and diversified its operations across various business areas such as Asset Management (Alfalah GHP Investment Management), Insurance (Alfalah Insurance) and Brokerage (Alfalah Securities). BAFL also has overseas operations in Bahrain, Afghanistan, Bangladesh and United Arab Emirates; these overseas operations cumulatively contributed 8.6% of the bank's pre-tax profits for 2018 (2017: 7.2%).

Strong board composition and experienced management team. Cost control and digital transformation continue to be important pillars in the bank's overall strategy.

Overall corporate governance framework is supported by strong board composition and oversight, professional management team and adequate control infrastructure. Well-structured strategic planning process is in place. Following several changes in key management positions, noted during our past review, there has been 3 new appointments in 2018. Cost control remains a fundamental part of BAFL's strategy. Going forward, key strategic areas include building customer base, Small & Medium Enterprise (SME) lending, transaction banking and shift towards digital banking (introduction of digital products such as mobile wallet).

Asset growth has remained flat

BAFL's asset growth remained flat in 2018, partly being attributable to the reduction in borrowings. Given a strategy of branch consolidation and deposit cost rationalization, BAFL's asset growth has lagged the growth rate of the private sector banks and the industry at large over the last 3 years (2016-2018); however, the bank's ADR remains the highest among peers. As a result, the bank's market share in the domestic deposit market has fallen following return on capital optimization strategy.

Given growth in lending operations, BAFL's ADR has increased and remains above the peer median

During 2018, the asset mix depicted some change, as fixed income government securities were offloaded, given expectations of monetary tightening. Taking into account the return on capital, the surplus liquidity was largely channeled towards the advances portfolio. Given the growth in advances portfolio, BAFL's ADR has increased and remained higher than peers as of Dec'18. In terms of segment exposures, corporate segment remains the mainstay of the lending operations. Nevertheless, healthy growth has been noted in Islamic and CBSME lending.

Asset quality indicators have improved over a timeline

The credit quality of the advances portfolio draws support from the fact that much of the portfolio constitutes corporate clientele, mainly large-sized blue-chip companies with very low probability of default. Overall counterparty concentration is within the acceptable threshold. Despite additional subjective classification, asset quality indicators have continued to improve, with gross infection falling to 3.6% as of Dec'18, which is aligned with the peer median. However, the drop in infection was also a result of the extra-ordinary portfolio growth. The bank does maintain adequate provisions, which provide NPL coverage of 0.87x, thus translated in net infection of 0.5% as at Mar'19.

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Given the heightened credit risk environment, some credit impairment is expected within the short to medium term horizon, which will test the underwriting quality of the industry. So far, as of Mar'19, we have not noted any material change in gross NPLs. VIS will continue to monitor these trends on a quarterly basis.

Given improvement in spreads and cost rationalization measures, RoAA has improved and stood slightly higher than the peer median.

In 2018, the bank's bottom line grew by 27% to Rs. 10.6b (2017: Rs. 8.4b). On a YoY basis, the RoAA has depicted improvement. The RoAA for 2017 was aligned with the peer median, albeit for 2018 it was slightly higher than the peer median. The bank achieved strong growth in revenues, by way of combination of volumetric growth in earning assets, improvement in spreads and healthy increase in ancillary income. On the other hand, the bottom line also benefited from the 2% YoY drop in operating expenses, as a result of which the bank's efficiency ratio has improved and has become aligned with peers.

Capitalization has been reinforced and comfortably complies with our criteria for 'AA+' rated banks

Given issuance of Rs. 7b Additional Tier I TFC in 2018, the bank's capitalization has been reinforced and the CAR, as of Mar'19, was comfortably compliant with our criteria for 'AA+' rated banks. Taking into account a slightly heightened growth rate, given the branch expansion envisaged in the ongoing year, the CAR is expected to remain compliant with our criteria, over the medium term horizon; however, this is sans the impact of IFRS 9 implementation, which we have not taken into account. As per the IFRS 9 impact analysis exercise conducted as of Dec'17, the impact was gauged as immaterial by the management.

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FINANCIAL SUMMARY			*(Rupees in millions)*
BALANCE SHEET	**2016**	**2017**	**2018**
Investments - Net	389,092.6	400,733.3	277,660.4
Advances - Net	378,720.3	400,655.4	501,636.5
Total Assets	929,645.7	998,827.9	1,006,217.8
Borrowings	178,311.0	207,193.7	123,738.24
Deposits & other accounts	634,740.0	644,985.0	702,895.3
Subordinated Loans	8,317.7	4,991.0	11,989.0
Tier-1 Capital	42,549.9	53,661.9	66,809.8
Net Worth (excluding deficit on revaluation of assets)	49,155.0	58,514.5	68,263.9
INCOME STATEMENT	**2016**	**2017**	**2018**
Net Mark-up Income	28,991.3	28,976.2	31,591.1
Net Provisioning	1,183.3	(616.4)	588.4
Non-Markup Income	8,907.3	9,076.1	10,200.4
Administrative Expenses	23,683.6	24,671.9	23,966.8
Profit Before Tax	13,023.2	13,705.2	16,837.8
Profit After Tax	7,899.9	8,367.3	10,625.2
RATIO ANALYSIS	**2016**	**2017**	**2018**
Gross Infection (%)	4.8%	4.2%	3.6%
Total Provisioning Coverage (%)	90.1%	94.0%	89.0%
Net Infection (%)	0.7%	0.5%	0.6%
Cost of Deposits (%)	3.06%	2.70%	3.10%
Net NPLs to Tier-1 Capital (%)	6.1%	3.5%	4.3%
CET 1 Capital Adequacy Ratio (CAR) (%)	9.86%	10.92%	10.90%
Tier 1 CAR (%)	9.86%	10.92%	12.17%
CAR (%)	13.18%	13.39%	14.95%
Markup Spreads (%)	2.90%	3.20%	4.51%
Efficiency (%)	66.7%	66.9%	59.0%
ROAA (%)	0.8%	0.8%	1.1%
ROAE (%)	16.5%	15.2%	16.8%
Liquid Assets to Deposits & Borrowings (%)	50.7%	46.9%	43.6%

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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.

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REGULATORY DISCLOSURES — Appendix III

Name of Rated Entity	Bank Alfalah Limited (BAFL)
Sector	Commercial Bank
Type of Relationship	Solicited
Purpose of Rating	Entity and TFC Rating
Rating History	

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
		RATING TYPE: ENTITY		
07/02/2019	AA+	A-1+	Stable	Reaffirmed
06/29/2018	AA+	A-1+	Stable	Reaffirmed
08/31/2017	AA+	A-1+	Stable	Reaffirmed
02/14/2017	AA+	A-1+	Stable	Initial

Rating Date	Medium to Long Term	Rating Outlook	Rating Action
	RATING TYPE: TFC (Tier 1)		
07/02/2019	AA-	Stable	Reaffirmed
06/29/2018	AA-	Stable	Reaffirmed
1/17/2018	AA-	Stable	Final
11/8/2017	AA-	Stable	Preliminary

Instrument Structure	Basel III compliant Tier 1, listed, perpetual, unsecured, subordinated, non-cumulative and contingent convertible debt instruments amounting up to Rs. 7.0b (inclusive of Green Shoe Option of Rs. 2.0b).
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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