RATING REPORT

Askari Bank Limited

REPORT DATE:
July 3rd, 2018

RATING ANALYSTS:

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RATING DETAILS

Rating Category	Latest Rating Long-term	Latest Rating Short-term	Previous Rating Long-term	Previous Rating Short-term
TFC-V	AA-		AA-	
Rating Outlook	Stable		Stable	
Rating Date	*June 29, '18*		*June 30, '17*	

COMPANY INFORMATION

Incorporated in 1991	External auditors: **M/s A.F. Ferguson & Co., Chartered Accountants**
Public Limited Company	Chairman of the Board: **Lt. Gen Syed Tariq Nadeem Gilani HI (M)(Retd)**
Key Shareholders (with stake 5% or more):	Chief Executive Officer: **Mr. Abid Sattar** (Subject to SBP approval)
Fauji Fertilizer Company Limited – 43.15%	
Fauji Fertilizer Bin Qasim Limited – 21.57%	
Fauji Foundation – 7.19%	

APPLICABLE METHODOLOGY(IES)

Commercial Banks Methodology (March 2018)-*http://jcrvis.com.pk/kc-meth.aspx*
Rating the Issue (June 2016): *http://jcrvis.com.pk/kc-meth.aspx*
Governing Linkages between Parent and Subsidiary Companies (Jan 2015): *http://jcrvis.com.pk/kc-meth.aspx*

Askari Bank Limited

OVERVIEW OF THE INSTITUTION

AKBL was incorporated in 1991. The parent entity of the Bank is Fauji Foundation which collectively owns 71.91% shares in the Bank. At end-FY17, the Bank has 516 branches including 91 Islamic banking branches and a wholesale bank branch in Kingdom of Bahrain.

Profile of Chairman

Lt. Gen Syed Tariq Nadeem Gilani HI (M) (Retd) became the Chairman of AKBL. He retired from armed forces in October 2015. He holds Masters degrees in War Studies from Quaid-I-Azam University, Islamabad and Strategic Studies from US Army War College, USA

Profile of CEO

Mr. Abid Sattar was appointed by the Board of Directors as President & Chief Executive of Askari Bank Limited in June'2018 subject to clearance from the State Bank of Pakistan (SBP). He is a seasoned banker with more than 35 years of domestic and international banking experience.

Financial Snapshot

Total assets: 1QFY18 – Rs. 619b; FY17– Rs. 657b; FY16 – Rs. 619b

Total equity: 1QFY18 – Rs. 33.0b; FY17 – Rs. 32.4b, FY16 – Rs. 32.6b

Net profit: 1QFY18 – Rs. 1.4b; FY17 – Rs.

RATING RATIONALE

The ratings assigned to Askari Bank Limited (AKBL) incorporate association with its primary shareholder, Fauji Foundation Group, a diversified conglomerate with strong financial muscle and presence in various sectors of the country. Operating as a mid-tier bank in Pakistan, AKBL enjoys a moderate footprint with a market share of around 4% both in domestic deposits and advances. After aggressive branch expansion pursued over the last few years, the bank largely consolidated branch network during FY17. The bank's enhanced outreach is likely to provide positive impetus to revenues and profitability in the medium-term. The ratings also derive comfort from continuous improvement in asset quality and effective management of spreads. The bank mitigated the risk of decline in spreads with increased credit financing towards higher yielding avenues and pursuing aggressive growth in low cost deposits.

Solid economic growth with pressure on external sector building up. Heating up of banking advances may affect asset quality: Pakistan's economy maintained an upward trajectory with GDP growth posting a ten year high of 5.3% during FY17. The aforementioned growth was underpinned by accommodative monetary policy stance, increase in development spending, renewed confidence in the private sector and improved energy supply. However on the downside, the surge in imports coupled with subdued level of exports resulted in current account weakening; the persistent increase in consumption oriented imports is an area of concern. These trends have increased dependence on external borrowings and heightened pressure on foreign exchange reserves. Subsequently, an international rating agency has changed the outlook on Pakistan's rating to 'negative' from 'stable' while maintained the rating at 'B3'. The outlook change was an outcome of increased external vulnerability risk and low foreign reserve adequacy hampering access to foreign funding at moderate costs. The financial intermediation demonstrated highest growth in over a decade during the outgoing year on account of low policy rate leading to expansion in private sector credit. The gross advances of banking sector posted an annual growth of 20.3% (FY16: 13.3%) to Rs. 6.6tr (FY16: Rs. 5.5tr) by end-FY17.

Given concentration in advances to private sector, asset quality indicators remain sound: The bank maintained a cautious advances growth strategy in order to conserve credit quality of loan book. Around 70% of the advances book comprised financing to private sector while the remaining were related to public sector entities. Corporate and Commercial portfolio remained the main driver towards credit expansion constituting two third of the advances book; meanwhile, growth was also supported by high yielding consumer segment. The advances portfolio of the bank mainly comprises fuel/energy, food & allied, sugar, textile, surgical, transport & communication, rice processing and real estate. Given moderate exposure in food and allied segment, stringent monitoring is required owing to overall depressed commodity prices. Increase in consumer financing was a function of higher disbursement to secured auto and home loans. Going forward, the management plans to sustain low risk appetite while expanding business volumes with major focus on government backed infrastructure projects. Moreover, with inauguration of first branch at Gwadar Port Authority together with dedicated China-desk in Islamabad and representative office in Beijing, the bank has positioned itself to acquire CPEC related business, going forward. The same is likely to positively impact AKBL's market share and profitability.

Investments size and types re-profiled in the wake of emerging interest rate scenario: Aggregate exposure in the sovereign / public sector manifested in investments & advances represents about 58% of total assets. On the other hand, barring textile in private sector financing, overall sectoral exposures remained diversified. Concentration of top-20 customers in the advances portfolio increased to 15% (FY16: 13%) by end-FY17. Improving trend in the credit risk profile of the bank continued during the outgoing year in line with decrease in gross infection and a modest

5.3b; FY16: Rs. 5.2b

increase in provisioning coverage. Credit risk emanating from investment portfolio is considered manageable given the sizeable proportion of government securities (95%) at end-FY17. Although reduction in duration of PIBs portfolio has been witnessed, the bank remains exposed to related market risk in an increasing interest rate scenario. Cognizant of the fact, the bank has reduced exposure in government securities to a certain extent by end-1QFY18. AKBL's listed equities stood at almost 10% of the bank's own equity base. While major exposure comprises blue chip companies, the bank remains exposed to market risk in a highly volatile stock market;

Sound Liquidity profile under a stable market share of deposits: Deposit base of the bank recorded a growth of almost 11% during FY17. In view of deposit growth, AKBL pursued a consolidation strategy by reducing proportion of term deposits to improve deposit mix and manage spreads. The bank largely maintained its market share in system deposits. The CASA deposits represented almost 85% (FY16: 82%) of the deposit base in line with expansion in outreach and branch network. Concentration in top 20 deposits increased to 15% (FY16: 12%) by end-FY17; however, liquidity profile of the bank is supported by presence of sizeable liquid assets in relation to deposits and borrowings and low advances to deposit ratio (ADR).

Stable profitability supported by improvements in cost of funds, operational efficiency and asset quality: Despite increase in scale of operations and higher net reversals against non-performing loans, the bank's operating and net profit remained largely stagnant mainly on account of lower gain on sale of securities. The spreads were maintained at prior year's level; decline in yield of mark-up bearing assets to 5.8% (FY16: 6.2%) was offset by subsequent decrease in cost of funds on the back of higher proportion of CASA deposits in the total deposit mix. The non-markup recurring income stood higher at Rs. 3.9b (FY16: Rs. 3.4b) in line with higher income from fee commission and foreign exchange dealings. As a result, efficiency (Admin cost to income) improve slightly during FY17. Going forward, the bank's primary focus will remain on mobilization of low cost deposits to ease pressure on spreads.

Capitalization level though adequate would need strengthening going forward: Capital Adequacy Ratio (CAR) stood lower (FY17: 12.1%; FY16: 12.5%) at end-FY17; the same is lowest amongst top and mid-tier banks. The increase in risk weighted assets was largely manifested in credit and operational risk weighted assets. The bank's tier-1 capital to risk weighted assets improved marginally to 9.3% (FY16: 9.1%) by end-FY17. With Basel III impending full implementation until Dec 2019~~;~~ regulatory requirement of CAR, inclusive of capital conservation buffer, will be 12.5%. The Bank is in process of raising ADT1 Capital to the tune of Rs. 6.0b to support its capital base. Net NPL to tier-I ratio of the bank depicted improvement on the back of lower NPL and higher tier-1 equity.

Management strengthening ongoing: Barring the position of President/CEO, overall stability at the senior management level was witnessed which has resulted in effective implementation of the business strategy for the bank. Subsequent to the resignation of previous CEO, Mr. Saleem Anwar, CFO, assumed charge as an acting CEO of the bank in March'18. Recently, Mr. Abid Sattar has been appointed as CEO of the bank, subject to clearance from the SBP.

Rating the Instrument: The bank has raised unsecured sub-ordinated loans through issuance of two 10-year Term Finance Certificates (TFC), TFC-IV and TFC-V, to support its capital adequacy ratio. The outstanding amount was Rs. 997.6m and Rs. 4.0b for TFC-IV and TFC-V, respectively at end-FY17. The liability of the TFC holders rank inferior to all other bank obligations including deposits. TFC-V carries a markup rate of 6m Kibor + 1.2% with an inbuilt call option exercisable after 5 years of issuance given SBP's approval. The maturity of TFC-V is Sep'24, whereas with approval of the SBP,TFC-IV has been redeemed on June 23, 2018 by exercising Call Option.

Askari Bank Limited (AKBL) ***(amounts in PKR billions)*** **Annexure I**

BALANCE SHEET	31-Dec-15	31-Dec-16	31-Dec-17	31-Mar-18
Total Investments	268.0	295.8	315.0	260.1
Advances- (net)	199.9	235.2	258.7	268.0
Total Assets	535.9	619.1	656.7	619.0
Borrowings	57.3	89.3	71.6	24.6
Deposits & other accounts	433.2	472.8	525.8	536.8
Subordinated Loans	5.0	5.0	5.0	5.0
Tier-1 Equity	21.8	25.4	27.4	28.7
Net Worth	26.9	32.6	32.4	33.0
INCOME STATEMENT	**31-Dec-15**	**31-Dec-16**	**31-Dec-17**	**31-Mar-18**
Net Mark-up Income	14.9	14.9	16.2	4.2
Net Provisioning/(Reversal)	0.9	-0.7	-1.2	-0.5
Non-Markup Income	6.7	7.2	6.3	1.2
Operating Expenses	12.3	14.3	15.2	3.9
Profit Before Tax	8.4	8.5	8.5	2.1
Profit After Tax	5	5.2	5.3	1.4
RATIO ANALYSIS	**31-Dec-15**	**31-Dec-16**	**31-Dec-17**	**31-Mar-18**
Market Share (Advances) (%)	4.7%	4.7%	4.3%	-
Market Share (Deposits) (%)	4.5%	4.2%	4.3%	-
Gross Infection (%)	13.8%	10.9%	9.4%	9.1%
Provisioning Coverage (%)	89.1%	92.4%	93.3%	92.1%
Net Infection (%)	1.7%	0.9%	0.7%	0.8%
Cost of deposits (%)	4.6%	3.7%	3.5%	-
Net NPLs to Tier-1 Capital (%)	15.7%	8.6%	6.5%	7.4%
Capital Adequacy Ratio (%)	12.5%	12.5%	12.1%	12.3%
Markup Spreads (%)	2.8%	2.4%	2.4%	-
Efficiency (%)	67.5%	77.7%	74.6%	72.2%
ROAA (%)	1.0%	0.9%	0.8%	0.9%
ROAE (%)	19.8%	17.5%	16.2%	16.9%
Liquid Assets to Deposits & Borrowings –repo adjusted (%)	58.5%	56.4%	56.8%	-

ISSUE/ISSUER RATING SCALE & DEFINITIONS

Annexure 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: JCR-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.jcrvis.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.jcrvis.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.

'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.jcrvis.com.pk/images/policy_ratings.pdf

'SD' Rating: An 'SD' rating is assigned when JCR-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	Askari Bank Limited
Sector	Commercial Banks
Type of Relationship	Solicited
Purpose of Rating	Instrument Rating

Rating History

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
		RATING TYPE: TFC-IV		
30-Jun-17	AA-		Stable	Maintained
29-Jun-16	AA-		Positive	Reaffirmed
30-Jun-15	AA-		Positive	Reaffirmed
18-Feb-15	AA-		Positive	Maintained
9-Sept-14	AA-		Stable	Initial
		RATING TYPE: TFC-V		
29-Jun-18	AA-		Stable	Maintained
30-Jun-17	AA-		Stable	Maintained
29-Jun-16	AA-		Positive	Reaffirmed
30-Jun-15	AA-		Positive	Reaffirmed
18-Feb-15	AA-		Positive	Maintained
9-Oct-14	AA-		Stable	Final
23-Sept-14	AA-		Stable	Preliminary

Instrument Structure

TFC-IV of Rs. 1b was issued in 2011, with a ten year term, repayable almost entirely in the last year in two equal semi-annual installments. The instrument was to mature on December 23, 2021 and carried profit rate of average 6M KIBOR + 175 bps in the first 5 years, with the spread to be enhanced to 220 bps in the subsequent 5 years. The TFC was an unsecured, privately placed, subordinated debt obligation, which had a call option that was exercisable after the first 5 years, subject to approval of SBP. The instrument was called on 23rd June’ 2018.

TFC-V of Rs. 4b was issued in 2014, with a ten year term, repayable almost entirely in the last year in two equal semi-annual installments. The instrument is set to mature on September 30, 2024 and carries coupon rate of average 6M KIBOR + 120bps. The TFC is an unlisted, privately placed subordinated debt obligation, which is convertible to common equity Tier-1, subject to approval by SBP. The instrument also has a call option which is exercisable after 5 years of issuance, subject to approval by SBP.

Statement by the Rating Team

JCR-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

JCR-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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