RATING REPORT

Meezan Bank Limited (MBL)

REPORT DATE:
July 01, 2019

RATING ANALYSTS:
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RATING DETAILS				
	Latest Rating		Previous Rating	
Rating Category	**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 28th' 18*		*May 30th, '18*	

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. – 30.0%	
Islamic Development Bank, Jeddah – 9.3%	
***as of the report date**	

APPLICABLE METHODOLOGY(IES)
PRIMER - Commercial Banks (November 2015):http://www.jcrvis.com.pk/Images/Meth-CommercialBanks201511.pdf

OVERVIEW OF THE INSTITUTION

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)

Noor Financial Investment Company Limited, Pakistan Kuwait Investment Company (Pvt.) Limited and Islamic Development Bank are the primary shareholders of the bank

Profile of Chairman

Mr. Riyadh Edrees serves as Chairman of the Board. Mr. Edrees holds more than 24years of experience at various organizations

Profile of CEO

Mr. Irfan Siddiqui is the founding President and CEO of the Bank. Mr. Siddiqui is a qualified Chartered Accountant from the Institute of Chartered Accountants of England & Wales.

RATING RATIONALE

Meezan Bank Limited (MBL) is the first and largest Islamic commercial bank of the country, accounting for 36% of total Islamic banking sector assets. Over the last decade, MBL has significantly expanded its operations; presently, MBL's distribution network is spread across 676branches, operating in more than 180 cities/towns across Pakistan. Consequently, the bank is 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 remain comparable to peers. MBLs strategy remains focused on branch expansion, which is planned to be further expedited in the ongoing year.

Major shareholding of the bank 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%).

MBL outgrew the domestic private banks and the industry at large. Asset mix has largely been maintained.

MBL outgrew the domestic private banks and the industry at large, wherein MBL's market share – in terms of assets - stood at 6.3% (Dec'17: 5.6%) and 4.8% (Dec'17: 4.3%) respectively. MBL's superior asset growth arose from the strong performance in both the retail and corporate deposit market. The asset mix has broadly been maintained. MBL's ADR[1], at 66.5% (2017: 64.3%), stands above the median ADR of 'AA+' rated banks. At the same time, MBL's liquid asset to funding ratio stands lower than the peer median.

Healthy growth in all financing segments. Going forward, focus on higher yielding Commercial & SME (CBSME) and Consumer segments is envisaged.

Gross advances recorded growth of 22% during 2018. The portfolio continues to be dominated by corporate clientele, which comprises about two-thirds of the financing exposures. Representation of corporate financing has slowly faded down over the years and is expected to gradually decline going forward. In contrast, the bank is focusing on CBSME and Consumer segments, which are relatively high/medium risk/return segments. Sector concentration in power, oil& gas, textile and agriculture persists, albeit in case of the latter two it has reduced.

Assets quality indicators have improved and compare favorably to peers.

Despite a rising credit risk environment – prevalent in the latter half of 2018 and continuing into the ongoing year – MBL has been able to maintain its asset quality. As of Dec'18, MBL's gross infection stood at 1.3%, comfortably below the peer group median of 3.6%. Furthermore, inclusive of general provisions, there are excess provisions against NPLs to the tune of 1.39x. However, given the strong focus on corporate clientele, the portfolio does depict counterparty concentration. Albeit, some comfort can be derived from fact that much of these exposures are government guaranteed, whilst the remaining exposures are outstanding against a corporate blue-chip clientele.

[1]For ADR calculation, Financings are net off SBP Islamic Export Refinance Scheme

Given the heightened credit risk environment, some credit impairment is expected over the short to medium term horizon, which will test MBL's underwriting quality. So far, as of Mar'19, the gross NPLs were almost at the same level as year-end 2018. VIS will continue to monitor these trends on a quarterly basis.

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.

MBL has managed to maintain profitability metrics, with RoAA trending in line with 'AA+' rated peer median.

Despite having limited liquidity placement avenues as an Islamic Financial Institution (IFI), which puts MBL at a disadvantage in comparison to its peers, the bank's profitability metrics trend in line with peers. However, with the recent issuance of PES-I Sukuk, profitability concerns of IFIs have subsided, as these Sukuk offer returns commensurate with conventional liquidity instruments.

In comparison to peers, MBL's profit strategy focuses on financing operations, as evident from a higher ADR vis-à-vis peers. In the outgoing year, MBL's net profit increased by 42% to Rs. 9.0b (2017: Rs. 6.3b). The growth in profitability is attributable to the volumetric growth in financing portfolio, along with a ~50bpts increase in spread and a healthy growth in fee & commission based income, mainly emanating from the growing trade finance business. Despite the expense base growing by 16%, MBL was able to reduce the efficiency ratio, which stood comfortably below the 'AA+' rated banks.

In the onset of significant monetary tightening, MBL is positioned to be a key beneficiary, as all financings of MBL have short re-pricing terms. Furthermore, given a significant CASA tilt of the deposit base, the cost of funding is also lower than peers.

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.

In 2018, the bank completed an additional Tier 1 Sukuk issue amounting to Rs. 7b. Post issuance of this instrument, MBL's CAR stands comfortably above the regulatory requirement and complies with our criteria for 'AA+' rated banks. From an equity standpoint, there is inherent counterparty exposure concentration. Given a rising interest rate environment, the bank's credit quality may deteriorate, which will test the adequacy of the capital buffers.

The present level of capitalization, along with the plans for further reinforcement in latter half of the year, deems the capital base as sufficient to withstand any non-performance events, excluding PSEs, which are essentially guaranteed by the GoP, and large-sized blue-chip corporate entities, wherein probability of default is very low. Furthermore, the impact of IFRS 9 implementation has been gauged as immaterial. In lieu of the same, and plans for further capital reinforcement in Q1'19, MBL's capitalization is expected to remain compliant with VIS criteria, for 'AA+' rated banks, over the medium-term horizon.

Meezan Bank Limited Appendix I

FINANCIAL SUMMARY			*(amounts in PKR billions)*
BALANCE SHEET	**DEC 31, 2016**	**DEC 31, 2017**	**DEC 31, 2018**
Total Investments	130.2	119.2	123.7
Gross Advances	319.6	428.8	522.2
Total Assets	662.1	788.8	937.9
Borrowings	32.0	36.8	36.4
Deposits & other accounts	559.4	667.2	785.5
Subordinated Sukuk (Tier II)	7.0	7.0	7.0
Subordinated Sukuk (Tier I)	-	-	7.0
Tier-1 Equity	27.5	33.6	46.6
Net Worth	30.4	35.0	40.3
INCOME STATEMENT	**DEC 31, 2016**	**DEC 31, 2017**	**DEC 31, 2018**
Net Mark-up Income	17.8	20.8	28.1
Net (reversal) Provisioning	(0.2)	1.3	1.1
Non-Markup Income	5.6	7.6	7.4
Administrative Expenses	14.7	16.6	19.2
Profit Before Tax	8.9	10.2	14.7
Profit After Tax	5.6	6.3	8.9
RATIO ANALYSIS	**DEC 31, 2016**	**DEC 31, 2017**	**DEC 31, 2018**
Market Share (Advances) (%)	5.7%	6.6%	6.6%
Market Share (Deposits) (%)	5.0%	5.4%	5.9%
Gross Infection (%)	2.1%	1.5%	1.3%
Provisioning Coverage (%)	118.1%	133.3%	138.9%
Net Infection (%)	0.08%	0.04%	0.04%
Cost of deposits (%)	2.4%	2.3%	2.6%
Net NPLs to Tier-1 Capital (%)	0.88%	0.50%	0.40%
Capital Adequacy Ratio (C.A.R) (%)	12.9%	12.9%	14.6%
Markup Spreads (%)	3.97%	3.93%	4.41%
Efficiency (%)	65.4%	60.7%	54.6%
ROAA (%)	0.93%	0.87%	1.04%
ROAE (%)	19.53%	19.26%	23.77%
Advances to Deposits Ratio (%)*	53.7%	61.0%	63.6%
Liquid Assets to Deposits & Borrowings (%)	51.5%	45.0%	44.4%
*For ADR calculation, Financings are net off SBP Islamic Export Refinance Scheme			

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: 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 — 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		
6/28/2019	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		
6/28/19	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		
6/28/19	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.
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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