

Report Date: July 3, 2013

| Ratings | Latest | Previous |
|---------|-------------|-------------|
| Entity | AA-/A-1+ | AA-/A-1 |
| Outlook | Stable | Stable |
| Date | Jun 28, '13 | May 21, '12 |

Sindh Bank Limited

Rating Rationale

Sindh Bank Limited (SBL) is wholly owned by the Government of Sindh, through its Finance Department. The bank was incorporated in Oct'10 and 2012 was the bank's second full year of operations. SBL benefited from a substantial start-up capital of Rs. 10b allowing the bank to post profitable results since inception despite pursuit of aggressive growth strategy. On account of growth in risk weighted assets, CAR of the bank has reduced since last review; however it is still substantial indicating room for further growth. Liquid assets carried on books are also sizeable vis-à-vis deposits and borrowings (adjusted for repo).

While access to retail deposits has increased in line with increasing footprint, concentration in deposits remains high. Dilution in deposit concentration levels may be expected as deposit volumes from 110 branches set up in 2012 increase. With another 40 branches to be set up in the on-going year, the bank is projected to have a network of 200 branches by year-end 2013. The bank has a widespread geographical footprint with branches functioning in all provinces; greater presence is observed in Sindh and Punjab. High cost Government of Sindh deposits reduced to 30% of total deposits (FY11: 78%) in FY12 and further to 27% by end 1Q13. Increase in non GoS deposits was higher than budgeted. Overall public sector deposits represent a sizeable portion of the total deposit base currently. Greater access to market based deposits has yet to be seen.

Concentration in the loan book remains high with a notable proportion of advances disbursed to the GoS Food Department guaranteed by GoS, while exposure against sugar sector, largely against pledge of stock, was also on the higher side. Top 20 loans comprised a notable proportion of the loan book with particularly high exposure against certain groups and companies. Portfolio quality has so far largely remained intact; high concentration in loans however exposes SBL to risk of capital erosion if larger counterparties undergo stress.

Investments largely comprised short term government paper carrying low credit risk and limited market risk. TFCs held in the portfolio are rated in the A band and above. Equity and mutual funds portfolio featured concentration; however, due to its low proportion in the investment mix risk arising on the same is manageable.

Profitability improved in FY12 on the back of improvement in spreads as the bank shed off high cost deposits. Spreads have however come under pressure in 1Q13 on account of reduction in return on markup bearing assets due to fall in discount rate; despite cost of deposits also having trended downwards. Efficiency ratio has weakened notably in FY12 and in 1Q13 and may remain under pressure as full year impact of branch opening costs is borne in the on-going year. In the long run, business volumes are likely to benefit from the enhanced footprint.

There has been turnover at the Board level and while largely this has been due to change in GoS nominees on account of changes at the government level; there has also been turnover in independent directors. Stability at the Board level may be required for effective governance and oversight. Internal audit function of the bank is being further strengthened to improve controls. Position of Head of Corporate and Investment Banking has remained vacant since last review. Head of SME has been assigned the task of supervising this function. The bank has expanded at a rapid pace; overall control environment has room for improvement as highlighted by auditors.

About The Institution:

Sindh Bank Limited was incorporated as a public limited unlisted company in October 2010. Government of Sindh has 100% shareholding in the bank. The bank had total branch network of 160 at end-2012.

Chairman: Mr. Muhammad Ejaz Chaudhry

President & CEO: Mr. M. Bilal Sheikh

Rating Analysts:

Zia M Usmani
M Omer Hussain