RATING REPORT

Sindh Bank Limited

REPORT DATE:
July 06, 2020

RATING ANALYSTS:
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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	
Date	*June 30, '20*		*June 21, '19*	

COMPANY INFORMATION

Incorporated in 2010	External auditors: **Naveed Zafar Ashfaq Jaffery & Co. 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 Commercial Banks Rating http://vis.com.pk/docs/Meth-CommercialBanks201803.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-2019.

Profile of the CEO

Mr. Imran Samad has more than 30 years of experience in Banks/FIs as President & CEO, Managing Director and as Senior Executive/Group Head in the many areas of banking functions. Prior to joining Sindh Bank, Mr. Samad worked at Bank AJK as President/CEO for around three years. He has also served as Acting Managing Director of Bank of Khyber and as Group Head.

RATING RATIONALE

Established in 2010, Sindh Bank Limited (SNDB) is a small sized public sector bank with Government of Sindh (GoS) as sole sponsor of the bank which is a key rating consideration. Headquartered in Karachi, the bank has a nation-wide branch network of 330 (2018: 300) branches; of which 14 are dedicated for Islamic banking. Market share, in terms of gross advances remains on the lower side vis-à-vis peers at 0.9% (2018: 1.0%).

During the outgoing year, senior management team has been strengthened with the appointment of a new CEO while fresh inductions were undertaken at the position of Head of Risk, Corporate & SME credits, Operations and Compliance. Moreover, management's efforts to strengthen governance and risk management framework is noted and considered important from a ratings perspective.

High exposure to credit risk and weak asset quality. Focus is on restructuring and recoveries while cautiously growing lending book.

Gross financing portfolio of SNDB has fallen slightly by ~3% during 2019 whereas due to sizeable provision undertaken net advances were reported significantly lower vis-à-vis preceding year. Corporate loan book continues to represent more than four-fifth of gross financing portfolio. Going forward, management plans to grow consumer and SME segments while quality of underwriting will be crucial as credit risk is higher in these segments. Overall client and sectoral concentration in financing portfolio remains on the higher side signifying sizeable exposure to credit risk.

While exposure to a single group (with significant exposure in Sugar) has been the major reason for deterioration in asset quality indicators over the years, non-performing loans (NPLs) have also emanated from other corporate exposures. NPLs after observing a fourfold increase in previous year, further increased by ~36% to reach Rs. 33.8b (2018: Rs. 24.9; 2017: Rs. 5.5b) while total provisioning coverage stood at 45.3% (2018: 22.3%). Provisioning coverage remains on the lower side due to FSV relaxation availed by the Bank. FSV benefit availed stood at Rs. 15.6b (2018: Rs. 8.57b) at end-Dec'2019.

While fresh NPL accretion is expected to remain limited due to 1 year principal extension by SBP and other regulatory relief measures issued by the government, provisioning charges are expected to remain elevated primarily due to FSV benefit expiry and also partly due to change in classification of NPLs (Around 90% of the NPLs were classified as loss as at end-March 2020). Resultantly, provisioning coverage is budgeted to increase to 58% at end-Dec'2020. Overall exposure to credit risk from the performing portfolio is considered high given the quality of exposures, weak macroeconomic indicators and sizeable slowdown expected in GDP growth due to impact of Covid-19. VIS expects already weak asset quality indicators to remain under pressure post expiry of principal extension period by SBP.

Shift in Investment strategy in 2019. Decline in interest rates has resulted in revaluation surplus on PIB portfolio.

SNDB's investment portfolio which reduced significantly in 2018 witnessed an increase by ~18% to reach Rs. 65.1b (2018: Rs. 55.3b) at end-2019. Growth in investment portfolio was largely funded by higher deposit base. Credit risk emanating from investment portfolio is considered limited as ~92% of investments are deployed in GoP securities. While investment in PIBs continued to represent the major portion of investments at end-2019, investment portfolio witnessed a shift from long-term fixed rate PIBs to short tenor T-Bills at end-1Q'20 in order to reduce exposure to market risk given the high benchmark rates. Proportion of T-Bills in total investment portfolio has increased to 32% (2018: 10%) at end-2019 and 45.4% at end-1Q'20. The PIB portfolio includes a mix of investments classified as AFS and HTM. Average rate on HTM PIB portfolio is significantly higher than benchmark rates while rate of AFS portfolio is close to market rates.

Average duration of PIB portfolio stood at 4.33 years. Total deficit on AFS investment portfolio stood at Rs. 2.9b (2018: Rs. 6.4b) at end-Dec'2019. However, the deficit has reduced considerably at end-1Q'20 while the portfolio recorded a surplus as of June 08, 2020. The total surplus on HTM and AFS portfolio was recorded at Rs. 1.25b and Rs. 192m, respectively as of June 08, 2020. Overall exposure to market risk has declined on a timeline basis. However, comfort is drawn from expected decline in inflation and interest rates which will result in further increase in revaluation surplus on PIB portfolio.

Liquidity profile draws comfort from sizeable liquid assets carried on the balance sheet while strong sponsor support is evident from sizeable deposits by GoS and related entities. Nonetheless, deposit mix and concentration have room for improvement.

Overall liquidity profile has witnessed significant improvement vis-à-vis preceding year on account of increase in liquid assets in relation to total deposits and borrowings (adjusted for repo). Deposit base, after a sharp decline in 3Q'19 has recovered with growth momentum continuing in the ongoing year, was reported at Rs. 155b at end-June'20. GoS and federal government entities continue to provide their support with sizeable deposits which constitute around three-fifth of total deposits. SNDB maintains a considerable cushion over regulatory requirements of Liquidity Coverage Ratio (LCR-268%) and Net Stable Funding Ratio (NSFR-160%). However, depositor concentration levels are high with top 50 depositors representing around one-half of total deposits. Moreover, deposit mix has room for improvement given that growth in deposit base has been through high yielding savings and fixed deposits.

Sizeable equity injection by sponsors has allowed the Bank to achieve compliance with regulatory capital requirements. Overall capitalization indicators remain weak due to significant un-provided NPLs. However, VIS expects strong support from sponsor to continue in future whenever the need arises to meet compliance levels.

Supported by the capital infusion of Rs. 11.7b during 2019, net equity improved to Rs. 17.1b (2018: Rs. 11.2b) at end-2019. SNDB achieved compliance with regulatory Capital Adequacy Ratio (CAR) on Dec'19, reporting at 13.2% (2018: 8.02%). Given the reduction in deficit on investment portfolio and decline in NPLs, profit posted in 1Q'20, CAR improved to 15.49% as at end-March 2020 which resulted in improvement in capital buffer. Moreover, the planned merger with an associate leasing company will further augment the bank's capital base by around Rs. 3.0b. This is expected to be completed in the ongoing year. Net-NPLs in relation to Tier-1 equity will remain on the higher side given that provisioning will be taken in a staggered manner over the years. While remaining compliant with regulatory requirement, capitalization indicators are expected to remain under pressure due to weak internal capital generation and continued provision against non-performing loans.

Trend in operating losses expected to continue. Sizeable provisions will continue to be a drag on profitability.

Given the full year impact of suspended income (compared to six months impact in 2018), higher NPLs arising in 2019 along with impact of low yielding PIBs vis-à-vis benchmark rate, spread of the bank reduced by half which resulted in significantly lower net mark-up income. The bank incurred an operating loss of Rs. 2,475.3m (2018: operating profit of Rs. 938.4m) in 2019. However, loss before tax was reported higher at Rs. 13.8b (2018: Rs. 1.4b) in 2019 on account of higher provisions. While quantum of operating losses has declined, trend in operating losses is expected to continue for some time.

Annexure-I	
Committee Names	**Members**
Risk Management Committee	- Mr. Javaid Bashir Sheikh (Chairman) - Mrs. Masooma Hussain (Member) - President/CEO (Member) - Head of Risk Management (Secretary)
Procurement, Information Technology & Security Committee	- Mr. Sami ul Haq Khilji (Chairman) - Mr. Anis A. Khan (Member) - President/CEO (Member) - Finance Secretary (GoS) (By Invitation) - Head of IT/ Head of Admin. (Secretary)
Human Resource & Remuneration Committee	- Mr. Anis A. Khan (Chairman) - Mr. Sami ul Haq Khilji (Member) - Finance Secretary (GoS) (Member) - President/CEO (By Invitation) - Head of HR (Secretary)
Audit Committee	- Finance Secretary (GoS) (Member) - Mrs. Masooma Hussain (Member) - Mr. Javaid Bashir Sheikh (Chairman) - Head of Internal Audit (Secretary)
Nomination Committee *	- Finance Secretary (GoS) (Member) - Company Secretary (Secretary)

**Nonfunctional due to lack of members.*

Sindh Bank Limited Appendix I

FINANCIAL SUMMARY				*(amounts in PKR millions)*
BALANCE SHEET	**Dec 31, 2019**	**Dec 31, 2018**	**Dec 31, 2017**	**Dec 31, 2016**
Total Investments	65,143	55,351	114,260	71,539
Advances	61,131	73,632	64,713	51,833
Total Assets	160,599	155,561	204,876	146,355
Borrowings	4,192	26,772	50,971	8,910
Deposits & other accounts	134,050	113,594	134,207	119,022
Paid-Up Capital	19,710	10,010	10,010	10,010
Tier-1 Equity	8,808	7,095	14,914	14,493
Net Worth	17,077	11,238	16,068	15,530
INCOME STATEMENT				
Net Mark-up Income	1,850	4,875	5,265	4,404
Net Provisioning	(10,020)	(1,378)	252	1,607
Non-Markup Income	(668)	(389)	1,328	3,495
Operating Expenses	4,922	4,527	4,157	3,864
Loss/Profit Before Tax	(13,761)	(1,419)	2,182	2,427
Loss/Profit After Tax	(8,260)	(1,205)	1,255	1,390
RATIO ANALYSIS				
Market Share (Advances) (%)	0.9%	1.0%	1.1%	1.0%
Market Share (Deposits) (%)	0.9%	0.9%	1.1%	1.1%
Gross Infection (%)	44.2%	31.4%	7.9%	2.8%
Net Infection (%)	30.3%	26.3%	7.4%	2.6%
Cost of deposits (%)	6.8%	4.2%	4.1%	4.5%
Capital Adequacy Ratio (C.A.R (%))	13.2%	8.0%	15.7%	17.5%
Markup Spreads (%)	1.4%	2.9%	3.3%	3.5%
Efficiency (%)	202%	83%	69%	78%
ROAA (%)	-5.2%	-0.7%	0.7%	1.0%
ROAE (%)	-58.3%	-8.8%	7.8%	9.5%
Liquid Assets to Deposits & Borrowings (%)	59.0%	47.2%	53.8%	68.9%

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.

REGULATORY DISCLOSURES	Appendix III
Name of Rated Entity	Sindh Bank Limited
Sector	Commercial Banks
Type of Relationship	Solicited
Purpose of Rating	Entity Rating
Rating History	(see table below)

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
RATING TYPE: ENTITY				
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.
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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Due Diligence Meetings Conducted	(see table below)

	Name	Designation	Date
1	Mr. Saeed Jamal Tariq	CFO	8-April-2020
2	Mr. Liaquat Ali	Head of Credit	8-April-2020
3	Mr. Dilshad Hussain Khan	SVP - Finance Division	8-April-2020