The Pakistan Credit Rating Agency Limited

Rating Report

National Bank of Pakistan

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
25-Jun-2022	AAA	A1+	Stable	Maintain	-
25-Jun-2021	AAA	A1+	Stable	Maintain	-
26-Jun-2020	AAA	A1+	Stable	Maintain	-
27-Dec-2019	AAA	A1+	Stable	Maintain	Yes
28-Jun-2019	AAA	A1+	Stable	Maintain	Yes
28-Dec-2018	AAA	A1+	Stable	Maintain	Yes
30-Jun-2018	AAA	A1+	Stable	Maintain	-
30-Dec-2017	AAA	A1+	Stable	Maintain	-
23-Jun-2017	AAA	A1+	Stable	Maintain	-
30-Jun-2016	AAA	A1+	Stable	Maintain	-

Rating Rationale and Key Rating Drivers

The ratings reflect formidable strength of National Bank of Pakistan (NBP) in the domestic commercial banking industry. The Bank's strong financial risk profile, characterized by, its share in the deposit base of the country, its firm risk absorption capacity and systemic importance provides strength to the ratings. NBP's strong domestic franchise along with extended outreach and high customer penetration aids the Bank in sustaining its position. NBP fortified its position as the second-largest bank in the country in terms of advances and deposits. The ratings are also driven by strong ownership structure (Government of Pakistan (GoP) holds majority stake) and healthy resource profile. The bank boasts of high proportion of current and savings account (CASA) deposits. There is a change at leadership position. Timely finalization of the key post is essential for long term and short-term standing of the bank. Advances observed an increase during CY21, mainly contributed to improving macroeconomic indicators. The bank has developed a system of for early warning pertaining to the risks of NPLs, as rise in NPLs is a concern, which must be managed via prudent exposure taking. In terms of absolute equity, the Bank stands at the first position in the industry. Furthermore, profitability of the Bank has witnessed a decline, with the Bank reporting profit after tax (PAT) of PKR 28bln for CY21 covered by decline in total income. With focused efforts, NBP Islamic Banking (Aitemad Islamic) has achieved a milestone of total assets worth PKR 100bln. Islamic Banking portfolio has also been well diversified to ensure better growth. Pakistan's economy has gone through several varied phases in last two years due to the COVID19 pandemic. Banking sector continued to flourish with high profitability. Going forward, the macro-economic environment is beset with myriad challenges due to heightened interest rate, tightening of demand, rupee depreciation and higher inflation. This has repercussions for all segments of the economy.

The ratings are dependent upon the management's ability to maintain the relative standing of the Bank in the industry in all key parameters. Cost optimization and sustenance in the asset quality is important as it will improve the profitability. Moreover, the Bank in a case related to pension benefits to retired employees has filed a review petition against the Supreme Court judgment and has also moved an application for the constitution of the larger bench which has been accepted.

Disclosure

Name of Rated Entity	National Bank of Pakistan
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology | Financial Institution Rating(Jun-21),Criteria | Correlation Between Long-term & Short-term Rating Scales(Jun-21),Criteria | Rating Modifiers(Jun-21)
Related Research	Sector Study | Commercial Bank(Jun-22)
Rating Analysts	Sehar Fatima | sehar.fatima@pacra.com | +92-42-35869504

Profile

Structure National Bank of Pakistan (NBP) was incorporated as a public limited company, under NBP Ordinance 1949 and is listed on Pakistan Stock Exchange (PSX).

Background NBP is the second largest lending institution in the country and provides banking services to all type of consumers in all fields of the economy. NBP is authorized to act as agent of State Bank of Pakistan (SBP) and handles treasury operations for Government of Pakistan (GoP). At the same time the Bank acts as a trustee of public funds.

Operations With 1,513 branches – including 189 Islamic branches – the Bank has the second largest branch network in Pakistan with all branches online with Core Banking Application (CBA). NBP also operates 19 overseas branches to cater the needs of locals as well as expatriates.

Ownership

Ownership Structure NBP is majorly owned (75.6%) by the Government of Pakistan (GoP), mainly through the SBP (75.2%). Other major shareholders include Foreign Companies (6.3%), Public Sector Companies (0.4%), and the general public (12.1%). The Bank's pattern of shareholding is illustrated in the adjacent table.

Stability Being the largest public sector commercial Bank, NBP is of strategic importance to the GoP. An implicit guarantee is provided against liabilities (deposits) of NBP under the Bank's (Nationalization) Act, 1974.

Business Acumen SBP, which has a major stake in NBP on behalf of GoP, to provide it with the industry-specific working knowledge and strategic capability as it has a holistic view of the entire industry.

Financial Strength The GoP has provided assistance to the Bank in the past and shall continue to support it as implicit guarantee is provided against liabilities (deposits) of NBP under The Bank's (Nationalization) Act, 1974. Apart from NBP, the parent bank (SBP) has a fully owned subsidiary with the name SBP Banking Services Corporation (SBP-BSC).

Governance

Board Structure According to BNA, 1974, the Bank is required to have a minimum of five members board at any point in time. The remaining Board consists of one non-executive director and seven independent directors including one independent director representing minority shareholders as required by the Code of Corporate Governance.

Members' Profile The board carries diversified experience including financial sector, particularly banking, civil services, and other businesses. Majority of the directors have above two decades of experience.

Board Effectiveness During CY21, 11 board meetings were held; attendance of directors remained high. Relatively, large number of meetings reflect continuous monitoring of affairs pertaining to oversee operations. High attendance of members reflects active oversight.

Financial Transparency The Audit Committee reports directly to the board. The Bank has joint External Auditors; Deloitte Yousaf Adil Chartered accountants and Grant Thornton Anjum Rahman Chartered accountants. Joint auditors expressed an unqualified opinion on the Bank's financial statements for the year ended December 31, 2021.

Management

Organizational Structure NBP has a lean organizational structure that clearly defines responsibilities, authority and reporting lines with proper monitoring and compliance mechanism. NBP has divided its functions into 20 departments, each of which reports directly to President, except the Audit & Inspection, which reports to Board Audit Committee.

Management Team NBP's senior management team comprises experienced bankers. Mr. Rehmat Ali Hasnie is acting president and CEO of the bank. He is serving in NBP since 2010 and has been the group chief of Inclusive Development Group (IDG) since 2019.

Effectiveness Functions of the management are clear and well-defined to effectively achieve its underlying goals and objectives. NBP has an effective mix of management committees that are established to monitor performance and assure the adherence to the policies and procedures.

MIS NBP uses "Profile" as its core banking application (CBA). The Bank is using Misys Kondor for Treasury function while, SAP is used for Financial General Ledger and Human Resources Management. The Bank has established a Payment Services & Digital Banking Group to develop business through alternate delivery channels.

Risk Management Framework RMG develops risk management policies and tools in line with SBP guidelines while ensuring implementation by respective departments. RMG has 8 functions; i) Credit Risk Architecture, ii) Enterprise Risk Management, iii) E-CIB and Data Management, iv) Operational Risk Management, v) Market & Liquidity Risk Management, vi) Business Process Review & COSO Project, vii) Information Security Division and viii) Credit Administration.

Business Risk

Industry Dynamics Pakistan's economy has gone through several varied phases in last two years. It was deeply impacted by the magnitude of the COVID19 pandemic. The economic activity revived afterwards and Pakistan posted a GDP growth rate of ~4.0% in FY21 after a contraction in economy of -0.4% in FY20 (GDP growth figures were revised after base year was changed from FY05-06 to FY15-16). Banking sector continues to flourish with high profitability. Banking sector weightage is approximately ~25% of the KSE 100 index. Total banking assets posted growth of ~19% YoY whilst investments surged by 21% YoY to PKR ~14.4trln (end-Dec20: PKR ~11.9trln). Gross Advances of the sector recorded growth (23%) to stand at PKR ~10.9trln (end-Dec20: PKR ~8.8trln). Non-performing loans witnessed slight uptick of 4% to PKR ~860bln. Capital Adequacy Ratio stood at 16.7% (regulatory requirement of 11.5%). During CY21, banking sector deposits enhanced to PKR ~21.6trln (grew by ~17%). Hence, ADR rationalized to 47% (end-Dec20: ~45%). Net profitability of the sector recorded at PKR ~267bln (CY20: PKR ~244bln); up 9% YoY. However, growth of equity base of the sector recorded meagre uptick of 0.8% YoY attributable to handsome dividend payout.

Relative Position NBP maintained its position as second largest commercial bank in the country in terms of customer deposits with a market share of 12.6% at end-Dec21 (end-Dec20: 12.0%). NBP maintains well diversified deposits and advances portfolio with no single sector having a major impact or control.

Revenues During CY21, the gross mark-up income of the Bank decreased by 10% to stand at PKR 231.8bln (CY20: PKR 257.8bln). Non-markup income of the Bank marginally raised by 2.4% to PKR 36.9bln (CY20: PKR 36.1bln). During 1QCY22, gross mark-up income reported at PKR 79.2bln (1QCY21: PKR 48.5bln).

Performance During CY21, NBP's asset yield decreased from 10.0% to 7.8%. Bank's cost of funds reduced to 4.5% (CY20: 5.9%). Consequently, the Bank witnessed a decrease in its net interest margin to 2.8% (CY20: 3.4%). Non-markup expenses for the year contracted by 4.9% to PKR 60.0bln (CY20: PKR 63.1bln). PAT reported at PKR 28.bln (CY20: PKR 30.6bln). During 1QCY22, profit after tax was recorded at PKR 9.8bln - highest in the banking industry.

Sustainability Going forward, NBP's key focus would be to enhance its lending book mainly through LSM sectors mainly textile, power & gas and metal products. At the same time, the management intends to explore new avenues in international operations to increase in deposit base, trade business and FI lending to reflect the improvement in funded and non-funded Income.

Financial Risk

Credit Risk As at end-Dec21, Gross advances of the Bank geared up by 13.2% to PKR 1,113bln (CY20: PKR 983bln). Advances to Deposits ratio (ADR) of the Bank decreased to 36.9% (CY20: 40.6%). Infection ratio of the Bank increased to 15.2% (CY20: 14.8%). During 1QCY22, infection ratio was recorded at 14.7%. Also, ADR of the bank rationalized to 45.1%.

Market Risk The Bank's investment portfolio constituting 55.2% of the total earning assets at end-Dec21 (end-Dec20: 53.9%). The mix of government securities in overall investments remained stagnant at 94.0%. As at end-Dec21, investments were increased by 9.1% to PKR 1,946bln.

Liquidity And Funding During CY21, Bank's liquidity ratio marginally decreased to 62.8% (63.5% at end-Dec20). The customer deposits base of the Bank registered an increase of 23.6% to stand at PKR 477.4bln. CASA mix of the Bank declined by a fair margin to 82.3% at end-Dec-21 (end-Dec20: 83.8%). During 1QCY22, bank's liquidity ratio further decreased to 61.8%.

Capitalization As at end-Dec21, Equity to total assets was recorded at 7.4% (end-Dec20: 8.9%). Both the Tier 1 ratio and total capital ratio stood at 15.4% and 20.4% respectively. As at end-Mar22, Tier 1 ratio and total capital ratio had remained constant up to 16.4% and 21.8% respectively.

PKR mln

National Bank of Pakistan Listed Public Limited	Mar-22 3M	Dec-21 12M	Dec-20 12M	Dec-19 12M
A BALANCE SHEET				
1 Total Finances - net	1,229,896	1,158,463	1,044,379	1,058,604
2 Investments	1,946,191	1,886,946	1,407,530	1,382,898
3 Other Earning Assets	159,966	368,145	158,507	183,602
4 Non-Earning Assets	395,395	426,976	403,367	493,488
5 Non-Performing Finances-net	9,472	6,154	(5,257)	5,798
Total Assets	3,740,921	3,846,684	3,008,527	3,124,389
6 Deposits	2,634,546	3,019,155	2,418,966	2,198,049
7 Borrowings	615,645	320,819	146,073	479,398
8 Other Liabilities (Non-Interest Bearing)	192,380	220,508	175,929	214,328
Total Liabilities	3,442,571	3,560,482	2,740,968	2,891,775
Equity	298,350	286,203	267,559	232,614
B INCOME STATEMENT				
1 Mark Up Earned	79,204	231,883	257,811	239,477
2 Mark Up Expensed	(53,412)	(134,265)	(153,656)	(167,570)
3 Non Mark Up Income	8,093	36,942	36,077	36,199
Total Income	33,884	134,559	140,232	108,107
4 Non-Mark Up Expenses	(16,755)	(60,004)	(63,112)	(65,853)
5 Provisions/Write offs/Reversals	(1,069)	(21,695)	(30,896)	(14,250)
Pre-Tax Profit	16,061	52,860	46,224	28,003
6 Taxes	(6,223)	(24,852)	(15,665)	(12,194)
Profit After Tax	9,837	28,008	30,559	15,810
C RATIO ANALYSIS				
1 Performance				
Net Mark Up Income / Avg. Assets	2.7%	2.8%	3.4%	2.4%
Non-Mark Up Expenses / Total Income	49.4%	44.6%	45.0%	60.9%
ROE	13.5%	10.1%	12.2%	7.2%
2 Capital Adequacy				
Equity / Total Assets (D+E+F)	8.0%	7.4%	8.9%	7.4%
Capital Adequacy Ratio	21.8%	20.4%	19.8%	15.5%
3 Funding & Liquidity				
Liquid Assets / (Deposits + Borrowings Net of Repo)	61.8%	62.8%	63.5%	56.3%
(Advances + Net Non-Performing Advances) / Deposits	45.1%	36.9%	40.6%	45.9%
CA Deposits / Deposits	50.9%	56.9%	54.4%	54.8%
SA Deposits / Deposits	28.6%	25.4%	29.4%	27.0%
4 Credit Risk				
Non-Performing Advances / Gross Advances	14.7%	15.2%	14.8%	12.9%
Non-Performing Finances-net / Equity	3.2%	2.2%	-2.0%	2.5%

Credit Rating

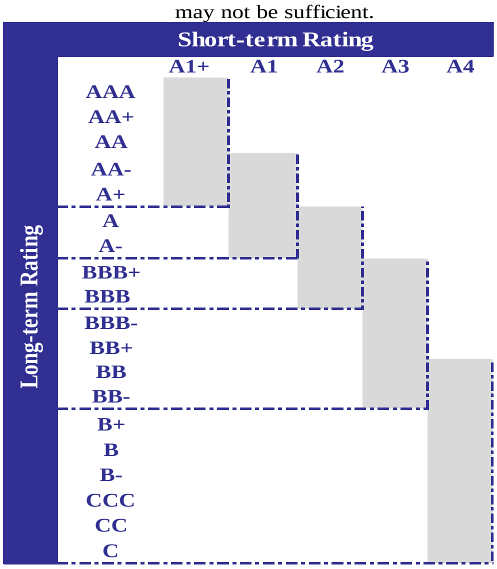
Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

Long-term Rating

Scale	Definition
AAA	**Highest credit quality.** Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments
AA+ AA AA-	**Very high credit quality.** Very low expectation of credit risk. Indicate very strong capacity for timely payment of financial commitments. This capacity is not significantly vulnerable to foreseeable events.
A+ A A-	**High credit quality.** Low expectation of credit risk. The capacity for timely payment of financial commitments is considered strong. This capacity may, nevertheless, be vulnerable to changes in circumstances or in economic conditions.
BBB+ BBB BBB-	**Good credit quality.** Currently a low expectation of credit risk. The capacity for timely payment of financial commitments is considered adequate, but adverse changes in circumstances and in economic conditions are more likely to impair this capacity.
BB+ BB BB-	**Moderate risk.** Possibility of credit risk developing. There is a possibility of credit risk developing, particularly as a result of adverse economic or business changes over time; however, business or financial alternatives may be available to allow financial commitments to be met.
B+ B B-	**High credit risk.** A limited margin of safety remains against credit risk. Financial commitments are currently being met; however, capacity for continued payment is contingent upon a sustained, favorable business and economic environment.
CCC CC C	**Very high credit risk.** Substantial credit risk "CCC" Default is a real possibility. Capacity for meeting financial commitments is solely reliant upon sustained, favorable business or economic developments. "CC" Rating indicates that default of some kind appears probable. "C" Ratings signal imminent default.
D	Obligations are currently in default.

Short-term Rating

Scale	Definition
A1+	The highest capacity for timely repayment.
A1	A strong capacity for timely repayment.
A2	A satisfactory capacity for timely repayment. This may be susceptible to adverse changes in business, economic, or financial conditions.
A3	An adequate capacity for timely repayment. Such capacity is susceptible to adverse changes in business, economic, or financial
A4	The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions. Liquidity may not be sufficient.



**The correlation shown is indicative and, in certain cases, may not hold.*

Outlook (Stable, Positive, Negative, Developing) Indicates the potential and direction of a rating over the intermediate term in response to trends in economic and/or fundamental business/financial conditions. It is not necessarily a precursor to a rating change. 'Stable' outlook means a rating is not likely to change. 'Positive' means it may be raised. 'Negative' means it may be lowered. Where the trends have conflicting elements, the outlook may be described as 'Developing'.

Rating Watch Alerts to the possibility of a rating change subsequent to, or, in anticipation of some material identifiable event with indeterminable rating implications. But it does not mean that a rating change is inevitable. A watch should be resolved within foreseeable future, but may continue if underlying circumstances are not settled. Rating watch may accompany rating outlook of the respective opinion.

Suspension It is not possible to update an opinion due to lack of requisite information. Opinion should be resumed in foreseeable future. However, if this does not happen within six (6) months, the rating should be considered withdrawn.

Withdrawn A rating is withdrawn on a) termination of rating mandate, b) the debt instrument is redeemed, c) the rating remains suspended for six months, d) the entity/issuer defaults., or/and e) PACRA finds it impractical to surveill the opinion due to lack of requisite information.

Harmonization A change in rating due to revision in applicable methodology or underlying scale.

Surveillance. Surveillance on a publicly disseminated rating opinion is carried out on an ongoing basis till it is formally suspended or withdrawn. A comprehensive surveillance of rating opinion is carried out at least once every six months. However, a rating opinion may be reviewed in the intervening period if it is necessitated by any material happening.

Note. This scale is applicable to the following methodology(s):

Entities

a) Broker Entity Rating
b) Corporate Rating
c) Financial Institution Rating
d) Holding Company Rating
e) Independent Power Producer Rating
f) Microfinance Institution Rating
g) Non-Banking Finance Companies (NBFCs) Rating

Instruments

a) Basel III Compliant Debt Instrument Rating
b) Debt Instrument Rating
c) Sukuk Rating

Regulatory and Supplementary Disclosure
(Credit Rating Companies Regulations,2016)

Rating Team Statements
(1) Rating is just an opinion about the creditworthiness of the entity and does not constitute recommendation to buy, hold or sell any security of the entity rated or to buy, hold or sell the security rated, as the case may be | Chapter III; 14-3-(x)

2) **Conflict of Interest**
i. The Rating Team or any of their family members have no interest in this rating | Chapter III; 12-2-(j)
ii. PACRA, the analysts involved in the rating process and members of its rating committee, and their family members, do not have any conflict of interest relating to the rating done by them | Chapter III; 12-2-(e) & (k)
iii. The analyst is not a substantial shareholder of the customer being rated by PACRA [Annexure F; d-(ii)] Explanation: for the purpose of above clause, the term "family members" shall include only those family members who are dependent on the analyst and members of the rating committee

Restrictions
(3) No director, officer or employee of PACRA communicates the information, acquired by him for use for rating purposes, to any other person except where required under law to do so. | Chapter III; 10-(5)
(4) PACRA does not disclose or discuss with outside parties or make improper use of the non-public information which has come to its knowledge during business relationship with the customer | Chapter III; 10-7-(d)
(5) PACRA does not make proposals or recommendations regarding the activities of rated entities that could impact a credit rating of entity subject to rating | Chapter III; 10-7-(k)

Conduct of Business
(6) PACRA fulfills its obligations in a fair, efficient, transparent and ethical manner and renders high standards of services in performing its functions and obligations; | Chapter III; 11-A-(a)
(7) PACRA uses due care in preparation of this Rating Report. Our information has been obtained from sources we consider to be reliable but its accuracy or completeness is not guaranteed. PACRA does not, in every instance, independently verifies or validates information received in the rating process or in preparing this Rating Report | Clause 11-(A)(p).
(8) PACRA prohibits its employees and analysts from soliciting money, gifts or favors from anyone with whom PACRA conducts business | Chapter III; 11-A-(q)
(9) PACRA ensures before commencement of the rating process that an analyst or employee has not had a recent employment or other significant business or personal relationship with the rated entity that may cause or may be perceived as causing a conflict of interest; | Chapter III; 11-A-(r)
(10) PACRA maintains principal of integrity in seeking rating business | Chapter III; 11-A-(u)
(11) PACRA promptly investigates, in the event of a misconduct or a breach of the policies, procedures and controls, and takes appropriate steps to rectify any weaknesses to prevent any recurrence along with suitable punitive action against the responsible employee(s) | Chapter III; 11-B-(m)

Independence & Conflict of interest
(12) PACRA receives compensation from the entity being rated or any third party for the rating services it offers. The receipt of this compensation has no influence on PACRA´s opinions or other analytical processes. In all instances, PACRA is committed to preserving the objectivity, integrity and independence of its ratings. Our relationship is governed by two distinct mandates i) rating mandate - signed with the entity being rated or issuer of the debt instrument, and fee mandate - signed with the payer, which can be different from the entity
(13) PACRA does not provide consultancy/advisory services or other services to any of its customers or to any of its customers' associated companies and associated undertakings that is being rated or has been rated by it during the preceding three years unless it has adequate mechanism in place ensuring that provision of such services does not lead to a conflict of interest situation with its rating activities; | Chapter III; 12-2-(d)
(14) PACRA discloses that no shareholder directly or indirectly holding 10% or more of the share capital of PACRA also holds directly or indirectly 10% or more of the share capital of the entity which is subject to rating or the entity which issued the instrument subject to rating by PACRA; | Reference Chapter III; 12-2-(f)
(15) PACRA ensures that the rating assigned to an entity or instrument is not be affected by the existence of a business relationship between PACRA and the entity or any other party, or the non-existence of such a relationship | Chapter III; 12-2-(i)
(16) PACRA ensures that the analysts or any of their family members shall not buy or sell or engage in any transaction in any security which falls in the analyst's area of primary analytical responsibility. This clause shall, however, not be applicable on investment in securities through collective investment schemes. | Chapter III; 12-2-(l)
(17) PACRA has established policies and procedure governing investments and trading in securities by its employees and for monitoring the same to prevent insider trading, market manipulation or any other market abuse | Chapter III; 11-B-(g)

Monitoring and review
(18) PACRA monitors all the outstanding ratings continuously and any potential change therein due to any event associated with the issuer, the security arrangement, the industry etc., is disseminated to the market, immediately and in effective manner, after appropriate consultation with the entity/issuer; | Chapter III | 18-(a)
(19) PACRA reviews all the outstanding ratings on semi-annual basis or as and when required by any creditor or upon the occurrence of such an event which requires to do so; | Chapter III | 18-(b)
(20) PACRA initiates immediate review of the outstanding rating upon becoming aware of any information that may reasonably be expected to result in downgrading of the rating; | Chapter III | 18-(c)
(21) PACRA engages with the issuer and the debt securities trustee, to remain updated on all information pertaining to the rating of the entity/instrument; | Chapter III | 18-(d)
Probability of Default
(22) PACRA´s Rating Scale reflects the expectation of credit risk. The highest rating has the lowest relative likelihood of default (i.e, probability). PACRA´s transition studies capture the historical performance behavior of a specific rating notch. Transition behavior of the assigned rating can be obtained from PACRA´s Transition Study available at our website. (www.pacra.com). However, actual transition of rating may not follow the pattern observed in the past | Chapter III | 14-(f-VII)
Proprietary Information