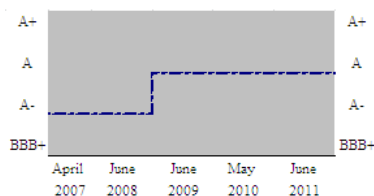


The Pakistan Credit Rating Agency Limited
RATINGS (JUNE 2011)
JS BANK LIMITED (JSBL)

	New	Previous
Entity		
Long Term	A	A
Short Term	A1	A1
Outlook	-	Negative

LONG-TERM ENTITY RATING HISTORY

FINANCIAL DATA

PKR (mln)

	1Q11	2010	2009
Total Assets	37,473	39,384	32,895
Equity	5,832	5,822	5,623
Net Income	10	(408)	(595)
Equity / Total Assets %	15.6	14.8	17.1
Net NPLs / Equity %	34.1	23.6	6.8
SBP CAR %	17.6	17.6	24.0

* Based on unaudited accounts for the 3 months ended March 31, 2011.

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RATING RATIONALE AND KEY RATING DRIVERS

- The ratings reflect the bank's strong liquidity and high capital adequacy, supplemented by a sound technological platform. The ratings recognize a geographically dispersed swiftly established branch network, which is expected to support building up of good franchise, in turn, low cost core deposit mobilization. However, recent infection in its loan book and yet to develop stable profitability are key concerns. Given the nascent stage of the bank and developing operational and control mechanism, identification and retention of key management personnel remains critical. To improve overall risks profile of the bank, the management, capitalizing on its increasing outreach, intends to deploy available funds in fundamentally sound business sectors, while establishing non-funded revenue stream.
- The bank's association with JS Group is a key concern. JSCL, the majority shareholder, demonstrating commitment, lately agreed to transfer a profit making entity (JS Global – 44% owned by JSCL) to the bank in swap of the bank's share. This would help the bank to meet immediate minimum capital requirement (MCR) i.e., PKR 7bln. For the next level of MCR, the bank, with limited internal generation, is exploring various options.
- The ratings are dependent on the bank's ability to achieve sustainable profitability while implementing its envisaged strategy. Meanwhile, any material deterioration in asset quality impacting the risk absorption capacity would negatively affect the ratings.

ASSESSMENT

- The macroeconomic landscape of Pakistan remains uncertain. Although a few indicators have improved as reflected in current account surplus of the country, prolonged energy crisis, stubborn inflationary pressure and burgeoning fiscal imbalance continue to pose major challenges to economic growth. This is also reflected in continuing weakening in the asset quality of the banks. The pace of accumulation of NPLs has stalled lately, but it would be challenging for the banks to maintain asset quality amidst subdued business sentiments.
- The deposit base of JSBL increased significantly (21%) during 2010, with yet to develop franchise, the major portion in deposit base comprises time deposits, followed by savings and demand accounts. The advances-to-deposits ratio of bank remained at moderate level (2010: 53%, 2009: 55%) which depicts the cautious stance of the bank for credit expansion. Going forward, the bank intends to increase the portion of low-cost accounts in overall deposit mix by capitalizing on expanding branch network while providing value added services which includes internet banking and visa debit cards. The increase in CASA will result in low cost of funds and in turn improve spreads.
- JSBL's mark-up income witnessed sizeable increase during 2010 in line with increase in earning assets, mainly government securities. Additionally, NIMR benefitted from improved spreads. Although fees, commission and brokerage income increased, other operating income witnessed a marginal decline on account of loss on sale of securities and decline in income from dealing in foreign currencies. Meanwhile, higher operating costs led to loss, despite a decline in provision expense. During 1Q11, the bank earned modest profit of PKR 10mln as compared to loss (PKR 189mln) suffered during same period last year. This profit is mainly attributable to improved spreads and other operating income. Moreover provision expense was low.
- The asset quality of the bank deteriorated significantly in the recent period; NPLs to gross advances ratio (1Q11: 14%, 2010: 13%, 2009: 7%). The increase is mainly due to the classification of Agritech Limited and Azgard Nine Limited (PKR 995mln; 52% of total NPLs). The bank has taken several initiatives to arrest the rising trend in the classified portfolio, which includes strict monitoring of watch-list accounts, elimination of stale limits in portfolio and restricting the value of shares offered as collateral. NPL coverage ratio is also low (10:28%, 2009: 56%). The exposure in Azgard Nine group may emerge as a significant drag on the bank's profitability in coming days, if material progress does not happen as currently the bank has not made any provisioning on this account. The bank has portfolio of listed and unlisted TFCs and Sukuks which represents 16% of finances – majority is in invested in entities operating in financial sector having sound credit ratings. However, a minor amount (PKR 300mln, 2% of total finances) represented investment in below investment grade at end-2010.
- Going forward, JSBL intends to diversify its revenue stream by focusing on primary dealership business, home remittances, and bancassurance. For lending, the bank will focus on margin financing, extending outreach to untapped areas like Faisalabad, Gujranwala etc., cross selling consumer products to corporate clients and by adopting effective pricing strategy to improve asset yield. Given the subdued economic conditions, improving spreads while managing related risks will remain critical for the bank.
- The bank implemented Temenos (T-24) as its core banking software. The software has supported the bank's branch expansion without any major hitches. Lately, the bank has implemented the Treasury Management Module and Know Your Customer module of T-24. The bank intends to further strengthen the technology platform.
- The losses during 2009 and 2010 have eroded the equity base of the bank. Resultantly, the bank issued ~202mln right shares at a price of PKR3 in Oct-10. In order to meet shortfall in MCR, the bank intends to increase share capital by issuing new shares to JS & Co. and other shareholders having investment in JSGL after acquiring stake in JSGL. Shareholders have approved the acquisition upto 71% of the shares of JSGL. Subsequent to completion of this transaction, the share capital of the bank will increase by around PKR 1,330-1,800mln depending on the extent of acquisition. Given the bank's weak performance, in the absence of sponsors support, meeting upcoming MCR from internal generation would be difficult (PKR 8,000mln end11, growing 1,000mln each year upto PKR 10,000mln).

PROFILE

- JSBL, incorporated in Mar-06, commenced operations on December 30, 2006. It operates through a network of 131 branches at end-Mar11, with its Head Office in Karachi. Listed on the Karachi Stock Exchange since 2007, it has three main business units: i) Retail and consumer banking, ii) Corporate and commercial banking, and iii) Treasury and investment banking. JSBL is a subsidiary (64%) of Jahangir Siddiqui & Co. Limited (JSCL).
- Mr. Jahangir Siddiqui, JS group's founder, chairs the bank's seven-member BoD (excluding the CEO). Mr. Kalim-ur-Rehman, the new CEO, has banking experience of over four decades. Given the nascent stage of the bank and still developing operational and control mechanism, identification and retention of key management personnel remains critical.