



State Bank of Pakistan

Banking Surveillance Department

Quarterly Performance Review of the Banking System

March 2009

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Quarterly Performance Review of the Banking System March 2009¹

1. Overview

Table 1.1: Highlights of the quarter ended Mar-09

	Mar-08	Dec-08	Mar-09
			Percent
Asset Growth	1.30	2.60	1.60
Advances Growth	4.30	3.70	(5.60)
Deposit Growth	0.80	3.80	0.03
Investments	6.80	5.20	20.00
Equity	0.70	4.20	1.50
Capital Adequacy Ratio	13.00	12.22	12.92
Capital to Total Assets	10.40	10.36	10.35
NPLs to Total Loans	7.70	9.13	11.54
Net NPLs to Net Loans	1.30	2.48	3.86
Return on Assets (Before Tax)	2.20	1.73	1.84
ROE (Avg. Equity & Surplus) (Before Tax)	20.70	16.74	17.70
Liquid Assets/Total Deposits	41.70	36.92	41.51
Advances to Deposits Ratio	72.30	75.94	71.69

The quarter under review is marked with the significant translation of weakened macroeconomic fundamentals on to the Pakistani banking system. The IMF's latest projections estimate that world GDP is likely to decline by 1.3 percent during 2009, while growth rate for Pakistan has also been revised down to 2.5 from 3.5 percent. Accordingly, the heightened credit risk transpired in significant increase in non-performing loans (NPLs) and associated asset quality indicators. Besides, the slowdown in economy dampened the growth rate of the banking system. However, banks largely maintained their resilience and registered improvement in key solvency indicators. The stress test results show that due to improvements in solvency position, the system maintains a strong resilience.

During the quarter under review, the asset base of the banking system passively grew by 1.6 percent. In the face of increased credit risk and resultant risk aversion on the part of banks as well as the lack of demand for bank credit from private sector, the asset mix of the banking system shifted away from loans and advances to risk-free govt. papers and govt. guaranteed bonds of PSEs. The loan portfolio (net) declined by 5.6 percent over the quarter while investments in govt. papers increased by 20 percent. As the banks' deposits remained stagnant, banks had to resort to interbank borrowings for financing the marginal increase in their asset base.

Besides the decline in loans and advances, the curtailed repayment capacity of the borrower also resulted in significant increase in NPLs, which registered an unprecedented over the quarter increase of 21 percent. However, the rate of this increase was not uniform among all

¹ The report presents performance of the banking system on the basis of unaudited Quarterly Report of Condition submitted by banks for the quarter ended 31st March, 2008.

banks, as a couple of banks contributed a substantial share of this overall increase.

Moreover, this unusually high increase also encompasses the external audit review adjustments for CY08. e.g. on account of subjective classification of loans rather than just based on time based criterion. The key asset quality indicators witnessed significant deterioration – infection ratio deteriorated to 11.5 percent (9.1 percent in Dec-08). Since major increase in NPLs occurred mainly in Doubtful category, which requires only partial provisioning coverage, the NPLs coverage as well as net infection ratios also deteriorated. Accordingly, the capital impairment ratio i.e. net NPLs to capital, went up to 17.9 percent for commercial banks, signifying that banks' inability to recover NPLs and further deterioration in their credit quality could impinge on solvency. Due to external audit review adjustments for CY08 that were directly recognized in the unaudited quarterly report of conditions for Mar-09, the retained earnings as well as the equity registered a slight contraction that was, however, more than covered by surge in revaluation surpluses on account of gains in revaluation of AFS securitites during the quarter. . The eligible regulatory capital showed improvements during the quarter, while shift in asset mix towards govt. papers reduced the value of the risk-weighted assets. Accordingly, capital adequacy ratio improved to 12.9 percent (12.2 percent in Dec-08).

Since the large share of additional provisioning requirements has been recognized in retained earnings through audited accounts for CY08, the earnings of the banking system for March-09 quarter remained largely immune. Banks posted before tax profit of Rs26.2 billion (Rs93.6 for the year 2008 and Rs28 billion for Mar-08). The bottom line registered a more than proportionate increase as compared with 2008 results, and baseline indicators of profitability i.e. pre-tax ROA registered a slight improvement to 1.8 percent (1.7 percent for 2008).

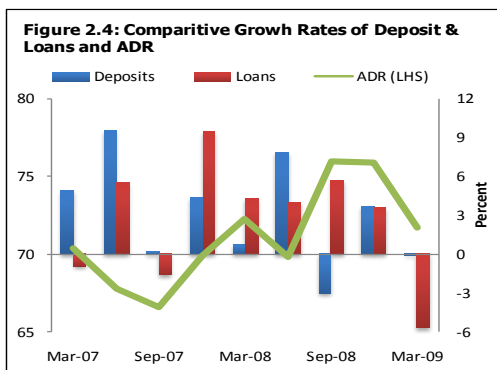
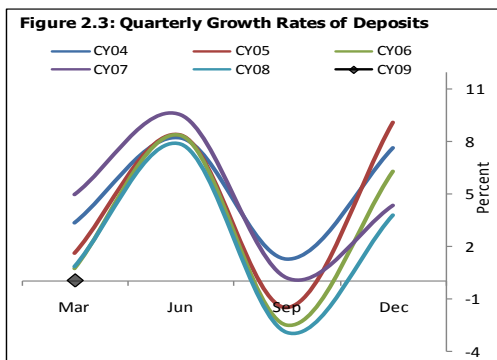
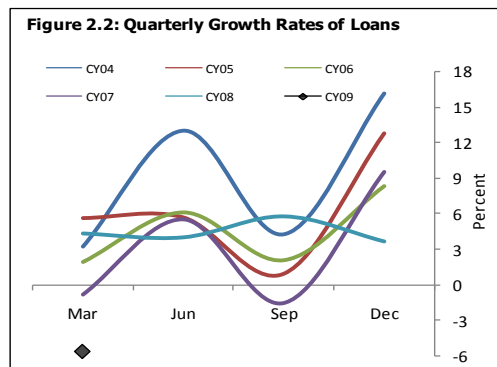
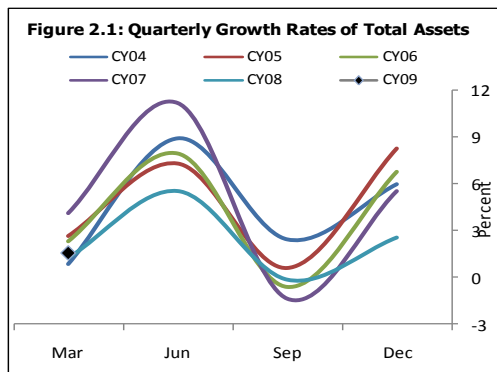
Banks' deposits remained stagnant during the quarter. After facing a significant deposit withdrawal during Sep-Oct 2008, the banks succeeded in recouping the deposit and posted a marginal increase by the end of Dec-08. During the quarter under review, banks' efforts for deposit mobilization were, however, largely muted by Central Directorate of National Savings (CDNS) products, which offer higher returns and greater security. Nevertheless, due to significant decline in loans and advances and increase in govt. papers the liquidity profile of the banking system further improved during the quarter. The market risk profile of the banking system also moderated. A strong recovery by the capital market made for a substantial part of the revaluation losses and enlivened the banks' interest in equity investments. Interest rate risk also remained subdued. Interest rates gradually declined during the quarter, thus appreciating the value of fixed income securities while re-pricing mismatches remaining within acceptable ranges.

Going forward, the impending economic slowdown and domestic securities issues may dampen the growth of the banking system in coming quarters. Low demand for banks' advances and increased risk aversion on the part of banks will further shift asset mix away from advances to Govt. papers. Banks will have to brace up their efforts for mobilizing the deposits, which are still showing stagnancy in the latest post quarter statistics. In the third week of April 2009, SBP cut the policy rate by 100 bps. Contrastingly, the interest rates have shown slight inch up in post announcement weeks as the credit demand for commodity operations picks up. However, this rise also indicates normalization of market conditions and KIBOR's tendency to restore its parity with discount rate that was disturbed after last quarter's liquidity stress. Nevertheless, in line with SBP monetary policy of gradual easing out, the interest rates are likely to remain relatively low.

The heightened credit risk will remain a fundamental area of concern for the banking

system in coming quarters. Nevertheless, the system is expected to remain profitable though the levels as well as the pervasiveness of earnings among different market players will remain constrained as compared to past years' results.

2. Asset and Funding Structure



The banking system continued to show the signs of slow down that has been prevalent for last one year or so. Asset base of the banking system grew by Rs91 billion (1.6 percent) over the quarter that has been lower than established trend of the first quarter which is marked with slow to moderate growth in asset base and its key components (see Figure 2.1).

Growth pattern and asset mix of the banking system usually follow an established trend. The latter half of CY08 however observed a deviation from the established trend. Significant rise in inflation rates pushing the real lending rates down and increased credit needs of the public sector enterprises kept the demand for bank credit alive during the entire CY08. During this period, however, growth in deposits remained lackluster. Deposits even experienced a sharp decline during third quarter and early months of last quarter of CY08, putting a significant liquidity strain on the banking system in October-November 2008. The situation somewhat normalized by the end of CY08; the quarter under review witnessed further easing out as the loans of the banking system declined by 5.6 percent over the quarter while deposit level remained intact and ADR came off significantly (see Figure 2.4).

In the face of increased credit risk due to deterioration in macroeconomic fundamentals and slowdown in economic activities, banks continued to re-profile their asset mix away from loans and advances to less riskier investments. Funds released from the retirements of loans were largely invested in govt. papers and govt.-guaranteed papers of PSEs. Resultantly, the share of advances in total asset declined to 52.6 percent (56.6 percent in Dec-08) and that of investments inched up to 22.6 percent (19.1 percent in Dec-08), corresponding to Mar-08 patterns. However, the level and composition of other asset components remained more or less stable over the quarter (see Figure 2.5).

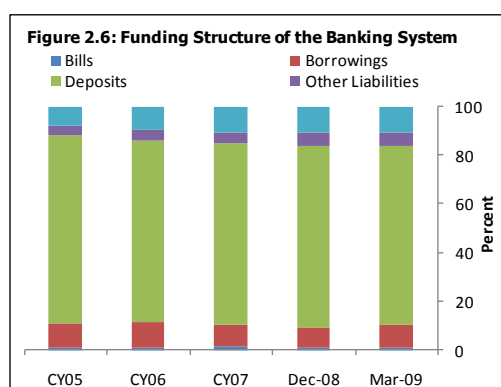
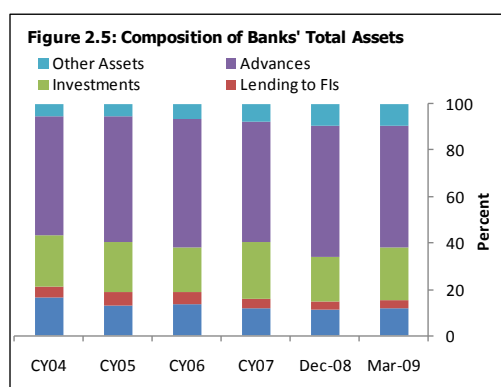
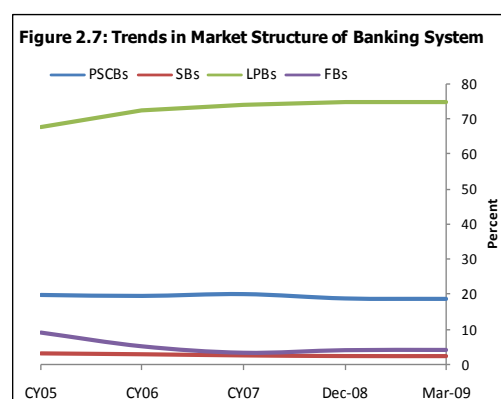


Table 2.1: Trends in Total Assets

	amount in billion Rupees					
	CY04	CY05	CY06	CY07	Dec-08	Mar-09
PSCBs	653	724	836	1,036	1,064	1,074
LPBs	1,980	2,483	3,102	3,836	4,229	4,302
FBs	304	339	224	173	232	239
CBs	2,937	3,547	4,162	5,044	5,525	5,615
SBs	106	113	120	127	128	129
All Banks	3,043	3,660	4,282	5,171	5,653	5,744



On the funding side, banks managed to finance the increase in their asset base largely through inter-bank borrowings as the deposits remained stable at the last quarter level while net worth increased marginally on aggregate basis. Resultantly, the funding structure slightly tilted towards borrowings, however the overall structure remained more or less stable and dominated by deposits followed by equity and borrowings (see Figure 2.6).

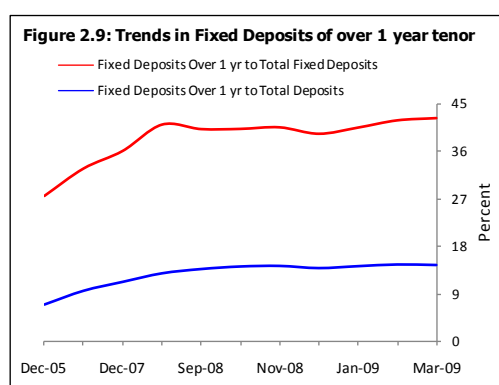
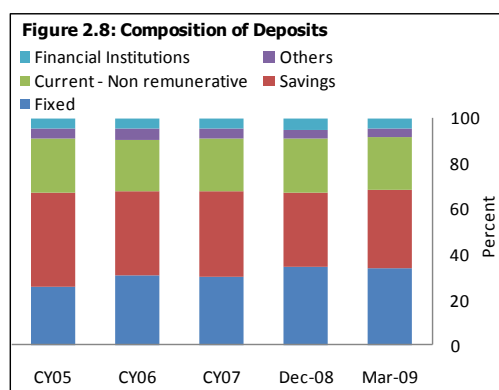
The group-wise analysis shows decelerated asset growth for all groups. The asset base of LPBs which hold 74.9 percent share of the market increased by 1.7 percent during the quarter. PSCBs that witnessed significant increase of 7.6 percent in their asset base during last quarter also grew by only 0.9 percent, while FBs grew at slightly faster rate of 3.4 percent. However, the overall market share of the groups with slight shifts remained almost intact at the last quarter's level (see Table 2.1 & Figure 2.7).

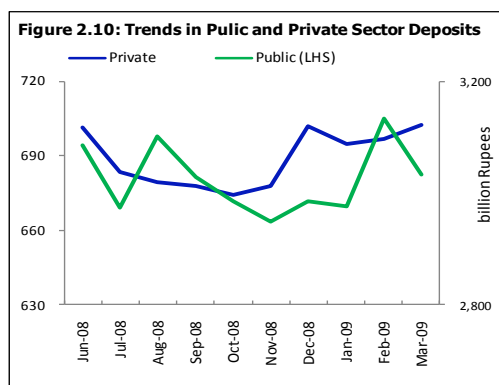
The banking system is marked with concentration as a fewer number of banks hold a major share of the system's total assets and deposits. This concentration has significantly reduced over the years as the medium-sized banks gradually gained market share. The market share of five large banks has gradually come down from 65 percent in CY96 to around 51 percent. Due to unusual liquidity stress during last quarter that affected mainly the small and medium sized banks, the market share of five large banks inched up to 52.4 percent (51.3 percent in Sep-08). During the quarter under review, this share receded back to 51.9 percent. Annex-II shows the market structure of the banking system on key financial indicators.

Deposits constitute the largest portion of banks' funding structure. The deposit component, which would witness a moderate to slow growth in first quarter, registered only a negligible increase of Rs1 billion and remained at Rs4,218 billion. This stagnation in deposits growth was mainly caused by the investors' increase preference for CDNS products which

offer higher returns and provide greater security, as the total investment in different CDNS products increased by Rs124 billion (11 percent) over the quarter. Since the asset base grew at a slightly faster pace and was largely financed by borrowings, the share of deposits in funding structure declined by 120 bps to 73.4 percent. Year-on-Year growth of 8.6 percent for Mar-09 quarter fell short of 15.5 percent growth for corresponding quarter of CY08; however, this growth was slightly higher than Year-on-Year growth in advances. Incidentally, foreign remittances, a key factor behind the recent years' strong growth in deposits, maintained the momentum. The remittances during the quarter under review grew at more than proportionate rate and were 21 percent higher than the remittances in corresponding quarter of the last year.

Though the level of deposits did not show any change, a disaggregated analysis of the deposits indicates quite dynamism in different components of deposits. Fixed deposits which were showing strong growth in recent quarters declined by 2.6 percent. Similarly, current accounts also contracted by 2.5 percent over the quarter. This withdrawal of fixed and current deposits was made up by savings accounts. Resultantly the composition of deposits shifted towards the savings accounts which again became the leading constituents of banks' overall deposits with 34.6 percent share followed by fixed deposits with 33.9 percent, and current accounts 23.3 percent (see Figure 2.8). The fixed deposits over the last couple of years have witnessed significant increase. This growth has been largely effected by SBP's policy drive to encourage the banks for mobilizing longer-term deposits so as to reduce maturity mismatches and liquidity risk. This policy of exempting long-term deposits, i.e. deposit with one year and above maturity, from CRR/SLR requirements has borne fruit by increasing the share of long-term deposits. Incidentally, the fall in fixed deposits during the quarter under review was largely caused by decrease in fixed deposits of less than three months tenor. However, the deposits with one year and above

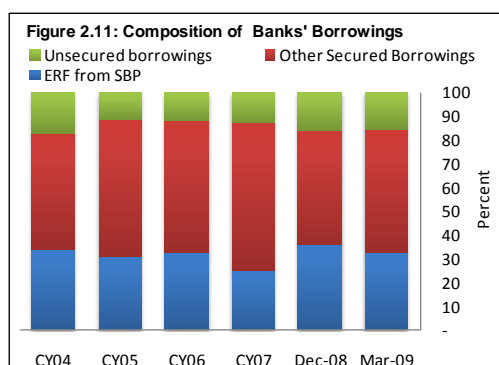




tenor have witnessed increase during the quarter (see Figure 2.9).

Composition of deposits by the type of depositor i.e. public and private sector has also varied during the recent quarters. The constrained fiscal position of the govt. put significant pressure on public sector deposits of the banks. Particularly, the banks having large public sector deposits faced significant liquidity pressures due to larger average size and higher volatility of these deposits (see Figure 2.10). It is estimated that since Jun-08 public sector deposits have registered a coefficient of variance of 0.021 vis-à-vis 0.017 for private sector deposits – the higher coefficient signifies greater average volatility in public sector deposits.

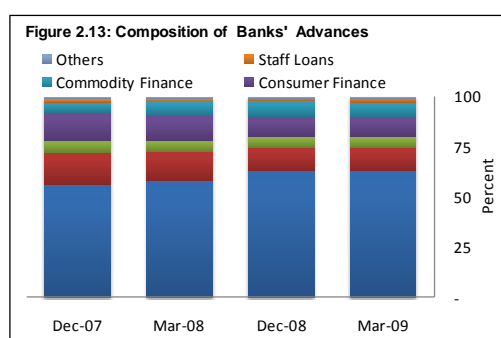
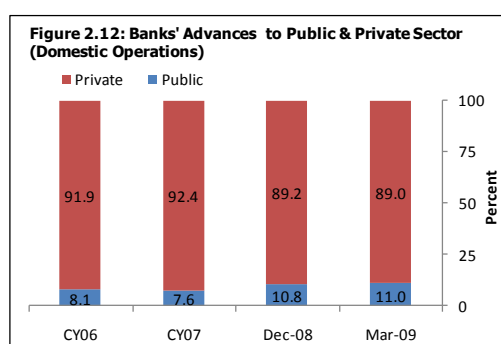
The marginal increase in asset was largely financed through increase in **borrowings** as deposit remained stable and net worth registered only slight increase during the quarter under review. Borrowings increased by Rs83 billion (17.8 percent) and their share in overall funding structure increased to 9.5 percent (8.2 percent in last quarter). Though all the components contributed towards this increase, however pronounced increase was observed in inter-bank repo borrowings which contributed 50 percent of the overall increase in borrowings. ERF borrowings, which on the back of number of incentive for export sector registered a significant increase during last quarter, further inched up by Rs12.2 billion (6.8 percent) while unsecured borrowings increased by Rs7.4 billion. Accordingly, the composition of borrowings further shifted towards secured borrowings (see Figure 2.11)



During the quarter under review, a number of banks paid dividend and recognized additional losses in their audited accounts for CY-08. These depletions were not recognized in quarterly report of condition for Dec-08 quarter, and have been now recognized directly into retrained earnings for Mar-09 quarter. Therefore, despite satisfactory earnings for the quarter, **Shareholders' Equity** lowered by 1.2 percent, and its share in asset base marginally

decreased to 9.4 percent (9.6 percent in Dec-08 and 8.7 percent in Mar-08). However, fresh equity injections and overall steady earnings led to YOY growth of 18.8 percent in the Equity. A general rise in interest rates and slump in stock market during the recent quarters had significantly marked down the value of both fixed-income and equity securities of banks. However during the quarter under review capital market registered significant improvement and interest rates lowered by the end of quarter, and the overall revaluation surpluses of the system inched up by Rs15.4 billion (35.5 percent), neutralizing the effect of decline in equity. Resultantly, the share of **net worth** (shareholders equity plus revaluation surpluses) in total assets remained at last quarter level of 10.4 percent (10.5 percent in CY07).

Advances (net) witnessed a significant decline of 5.6 percent over the quarter that was in sharp contrast to industry's established patterns for the first quarter during which the advances would grow at moderate to slow pace (see Figure 2.2). This decline largely highlights the banks' realignment of their risk profiles and asset mix to cope with the building credit risk in the backdrop of emerging vulnerabilities in the macroeconomic environment both at home and across the globe. Last year witnessed a strong growth in bank credit, loan increasing by 18.9 percent (12.7 percent in CY07) while deposit growing at 9.5 percent. Besides, the increased demand from private sector, this growth was significantly influenced by heightened credit consumption by public sector enterprises, which accounted for 28 percent of this increase in advances. During the quarter under review, both private and public sector reduced their borrowings from banking sector. However, the decline was relatively slower in banks' lending to public sector, resultantly, the share of public sector advances in total advances inched up to 11 percent (see Figure 2.12). Segment wise analysis² shows that all segments viz. Corporate, SME, Consumer, Agriculture and



² The following analysis of composition of advances and shift therein is based on the banks' domestic operations only.

Figure 2.14: Composition of Consumer Loans Mar-09

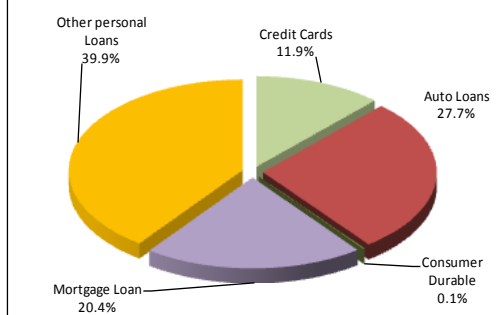


Table 2.2: End-use of Advances (net)

	amount in billion Rupees, share in percent					
	Dec-07		Dec-08		Mar-09	
	Amount	Share	Amount	Share	Amount	Share
Fixed Investment:	609.2	22.6	738.1	23.1	731.7	24.0
Corporate Sector	549.0	20.3	694.2	21.7	691.1	22.7
SMEs	60.3	2.2	43.9	1.4	40.6	1.3
Trade Finance:	415.9	15.4	480.6	15.1	459.6	15.1
Corporate Sector	348.0	12.9	438.3	13.7	420.3	13.8
SMEs	67.9	2.5	42.3	1.3	39.2	1.3
Working Capital:*	1,231.6	45.6	1,562.9	49.0	1,461.8	48.0
Corporate Sector	623.2	23.1	883.3	27.7	817.1	26.8
SMEs	309.1	11.4	288.8	9.0	269.3	8.8
Agriculture	150.8	5.6	155.5	4.9	150.7	4.9
Commodity Financing	148.4	5.5	235.4	7.4	224.7	7.4
Consumer Finance:	371.4	13.8	332.2	10.4	316.7	10.4
Credit Cards	46.8	1.7	40.7	1.3	37.8	1.2
Auto Loans	111.4	4.1	95.3	3.0	87.6	2.9
Consumer Durable	1.1	0.0	0.3	0.0	0.3	0.0
Mortgage Loan	67.4	2.5	66.9	2.1	64.6	2.1
Other personal Loans	144.7	5.4	128.8	4.0	126.4	4.1
Staff Loans:	52.2	1.9	64.5	2.0	66.7	2.2
Housing Finance	36.8	1.4	46.7	1.5	47.7	1.6
Others	15.4	0.6	17.8	0.6	19.1	0.6
Others	20.6	0.8	13.5	0.4	12	0.4
Total	2,700.9	100.0	3,192	100.0	3,048	100.0

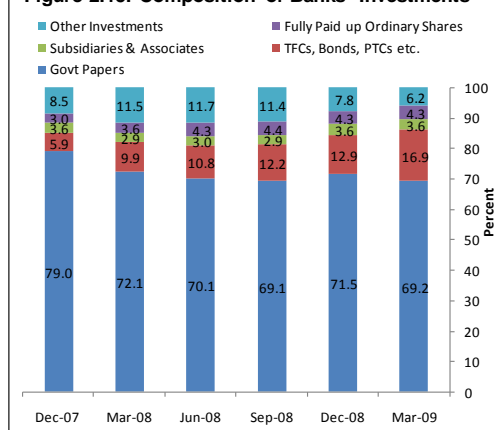
* agriculture and commodity finance are added in this category for analysis in this section only.

Commodity Operations experienced decrease during the quarter. In line with its leading share in lending portfolio, corporate sector contributed around 61 percent of the overall decline in loans and advances. Decline in other segment were also proportional to their share in overall lending portfolio. Therefore, the composition of lending portfolio remained stable at last quarter's levels, with share of SME slightly contracting during the quarter (see Figure 2.13). Analysis by end use of advances also reflects decline across almost all end uses. Working capital finance, being the largest component, contributed the largest chunk of decline in advances. Only staff loans witnessed a marginal increase; however, their share remains minute in overall lending portfolio.

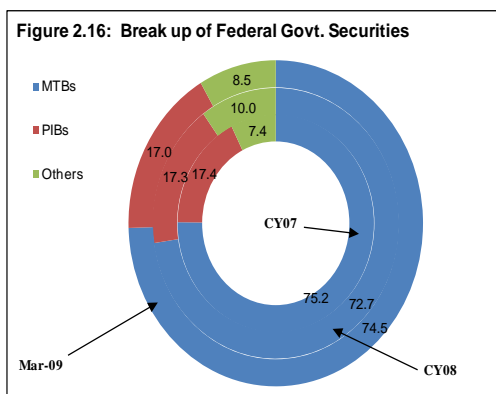
The **consumer finance** after showing a strong and persistent increase up till the end of CY07 has been gradually declining since then. During the quarter under review consumer portfolio further reduced by 4.6 percent and its share in the overall lending portfolio remained at 10.4 percent (see Table 2.2). The breakup depicts that all consumer finance categories contracted during the quarter; however, the decline was most significant in Auto Loans category that came down by 8.0 percent. However, the internal composition of the consumer finance largely remained stable, with Personal Loans contributing the largest share followed by Auto and Mortgage Loans (see Figure 2.14).

Investments, the second largest component of the banks' asset base, grew at a strong pace i.e. 20.0 percent (Rs216 billion) during the quarter under review. Investments had followed a declining trend since the last quarter of CY07. However, this trend reversed during the last quarter as investment portfolio (net) increased by 5.2 percent. During the quarter under review, this trend further invigorated as the banks were re-profiling their asset mix in the face of heightened credit risk. This increase was largely contributed by investment of Rs130 billion in Govt. papers and Rs81 billion in Bonds, Term Finance Certificates (TFCs), and Participation Term Certificates (PTCs). The

Figure 2.15: Composition of Banks' Investments



growth in the latter component was relatively pronounced, as banks invested heavily in govt. guaranteed TFCs of power distribution companies. Accordingly, the internal composition of investments shifted towards Bonds, TFCs, & PTCs, but remained highly dominated by Govt. papers (see Figure 2.15). The capital markets registered a strong recovery as KSE-100 index rose by 17 percent during the quarter, highlighting the restoration of investors' confidence. Accordingly, equity investments of banks also witnessed a strong increase of Rs9.6 billion (20.7 percent) and maintained their share in overall investment portfolio of the banking system. The internal composition of govt. papers shows slight increase in banks' preference for short-term MTBs over long-term PIBs, which are more prone to mark-to-market losses and have limited SLR eligibility. However, investment in both these papers registered increase: 19.8 percent for MTBs and 14.6 percent for PIBs, increasing the share in overall composition (see Figure 2.16).



Going forward, the impending slowdown in economic activities will continue to dampen the growth rate of the banking system. The private sector is not likely to put significant demand for bank credit, while increased credit needs of the public sector is likely to make for this low demand from private sector. Accordingly, the asset composition is likely to shift towards investments, particularly the govt. papers. However, wooing back the depositor towards banking system will remain a major challenge for the banks, as in the post quarter weeks deposits base continues to show the signs of stagnancy.

3. Financial Soundness of the Banking System

3.1 Solvency³

Table-3.1.1: Capital Adequacy Indicators

Percent	Basel-I				Basel-II*	
	CY04	CY05	CY06	CY07	Dec-08	Mar-09
CAR						
PSCBs	13.4	14.5	15.2	17.4	12.8	14.0
LPBs	10.1	10.6	12.7	12.8	12.2	12.7
FBs	17.4	16.4	15.0	13.5	19.8	22.4
CBs	11.4	11.9	13.3	13.8	12.6	13.3
SBs	(9.0)	(7.7)	(8.3)	(7.8)	(2.3)	(2.5)
All banks	10.5	11.3	12.7	13.2	12.2	12.9
Tier 1 Capital to RW						
PSCBs	8.6	8.8	11.1	13.0	10.1	11.4
LPBs	7.5	8.3	10.4	10.5	10.3	10.7
FBs	17.1	16.1	14.3	12.9	19.3	21.9
CBs	8.6	9.1	10.7	11.1	10.7	11.3
SBs	(15.0)	(13.6)	(13.3)	(13.5)	(7.6)	(7.5)
All banks	7.6	8.3	10.0	10.5	10.2	10.8
Capital to Total Assets						
PSCBs	8.7	12.6	12.2	13.7	11.9	11.1
LPBs	6.5	7.0	9.2	10.2	10.1	10.3
FBs	8.9	9.5	10.1	11.2	13.9	14.4
CBs	7.2	8.4	9.9	10.9	10.7	10.6
SBs	(9.4)	(8.1)	(8.0)	(5.5)	(2.5)	(2.7)
All banks	6.7	7.9	9.4	10.5	10.4	10.3

Figure 3.1.1: Risk-Based Capital Position

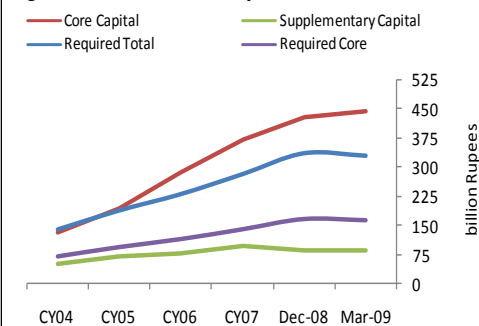
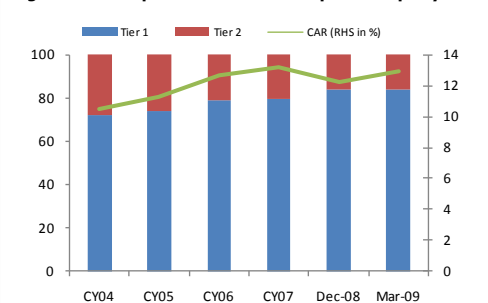


Figure 3.1.2: Capital Structure and Capital Adequacy



Solvency position of the banking system witnessed improvement during the quarter under review. The CAR of the banking system improved to 12.9 percent up by 0.7 percentage points (12.3 percent in Mar-08) due to increase in eligible capital and decrease in Risk Weighted Assets (RWAs). However, hazard to the solvency from heightened credit risk significantly increased over the quarter (see Table 3.1.1).

The composition of eligible capital shows that the qualifying risk-based capital of the banking system increased to Rs532.6 billion in Mar-09 from Rs512.8 billion in Dec-08 (see Figure 3.1.1). The core capital, being the mainstay of banks' capital rose by 3.7 percent to 83.6 percent in Mar-09. The trend of strengthening of the core capital to total capital has been continuing since CY04, when the ratio was 72.2 percent (see Figure 3.1.2). Further analysis of the core capital shows that the shareholders' equity, which is its key component, declined by 1.2 percentage points over the quarter (18.9 percent increase on YoY basis), mainly on account of recognition of losses as well as payment of dividends by some banks for CY08. However, this decrease in shareholders equity has been more than offset by reduction in compulsory deduction such as revaluation deficits and investment in associates, due to improvement in capital markets and the decrease in interest rate. As a result, the core capital of the banking system improved over the quarter. The increase in core capital was complemented by 3.2 percent increase in supplementary capital during the quarter under review (see Figure 3.1.1).

The CAR has been further strengthened by 1.9 percent decrease in RWA over the quarter. The

³ The above discussion is based on the CAR calculations on Basel-II framework. Except for three SBs which are reporting on Basel-I reporting formats, all other banks have reported on Basel II. These three banks hold 0.4 percent of the banking systems assets.

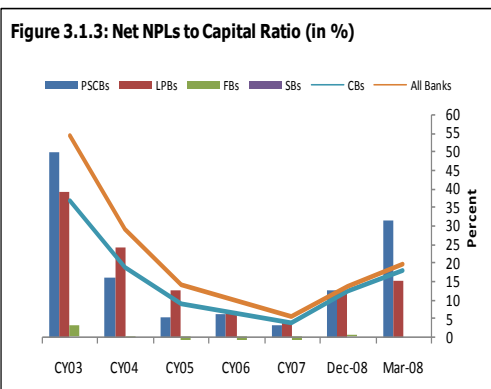
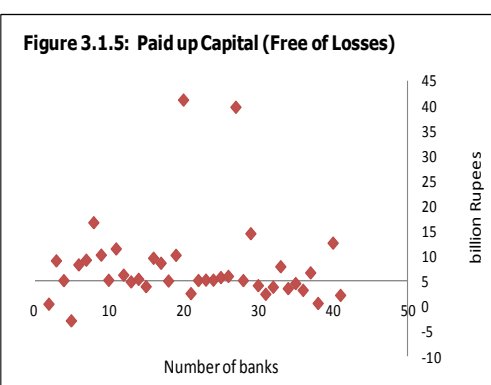
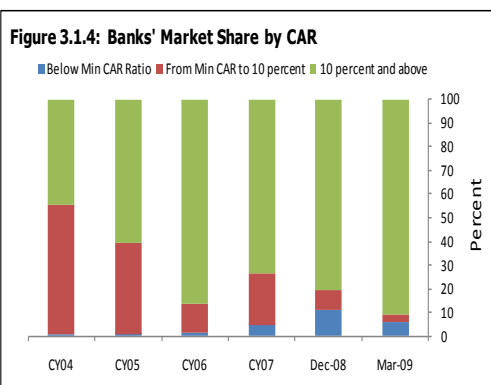


Table-3.1.2: Distribution of Banks by CAR

	Total	Below Min CAR Ratio*	From Min CAR to 10%	10 to 15 %	Over 15 %
CY04	38	1	13	9	15
CY05	39	2	7	13	17
CY06	39	3	4	15	17
CY07	39	3	6	12	18
Dec-08	40	4	2	13	21
Mar-09	40	4	1	13	22

* From December 31, 2008, banks are required to maintain minimum CAR of 9 percent instead of previous requirement of 8 percent.



decline is reflective of the risk-aversiveness of the banks as advances decreased by 5.6 percent, while the investments, mostly in Govt. securities, increased by 20 percent during the quarter (9.24 percent YoY). The change in composition of the various components of the RWA also confirms the above trend; Credit Risk Weighted Assets, the major source of RWA, declined by 100 bps to 83.7 percent over the quarter.

Both the factors viz; increase in eligible capital and decrease in RWA, lead to improvement in solvency indicators. The CAR of the system improved to 12.9 percent, while the Core Capital to RWA increased to 10.8 percent (9.7 percent in Mar-08). The capital to total assets ratio remained intact at 10.4 percent in Mar-09. With capital to total ratio at 6.7 percent in CY04; improvement over the years reflects increase in the stake of owners that bode well for the overall solvency of the banking system (see Table 3.1.1).

Group-wise position shows that CAR of all the groups increased except for SBs. The capital adequacy of PSCBs which declined to 12.8 percent in CY08 witnessed increase by 1.3 percentage points during the quarter under review. (see Table 3.1.1).

Though the decreasing advances improved the CAR of the system; however, weakening asset quality had impacted the capital impairment ratio i.e. net NPLs to Capital. The ratio increased by 6.1 percentage points to 19.6 percent, after bottoming out in CY07, reflecting increased threat to solvency from heightened credit risk (see Figure 3.1.3).

The disaggregated analysis shows that 36 banks have CAR above 9 per cent (see Table 3.1.2). The market share of banks having CAR of 10 percent and above stood at 90.9 percent in Mar-09, whereas 94.5 percent of the banking system assets rest with the banks having CAR of 9 percent and above (see Figure 3.1.4). Further, 30 banks including 5 foreign banks are fully compliant with the MCR (see Figure 3.1.5). Most of the remaining banks are in the process

of meeting the MCR, while 4 of these banks are under the process of restructuring/privatization.

The solvency position of the banking system has thus far shown sign of strength. However, deteriorating asset quality threatens to transmit into the solvency indicators. In line with the global slowdown in growth and capital accumulation by financial institutions, SBP has rationalized the minimum paid up capital and risk based capital adequacy requirements.⁴. Nevertheless, SBP's policy to enhance the solvency of the banking system has significantly strengthen the capital base of the banks and provided them sufficient cushion to withstand shocks.

⁴ See BSD Circular No. 30 of 2008 and 7 of 2009.

3.2 Profitability

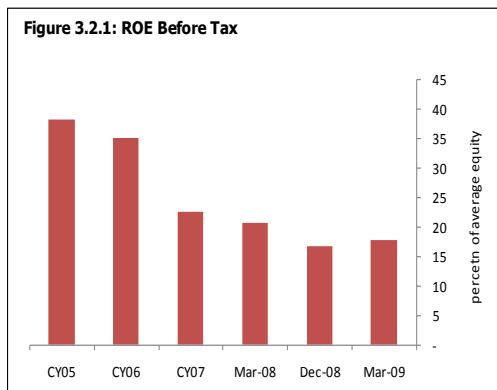
Table 3.2.1: Profitability of Banking System

	amount in billion Rupees						
	CY04	CY05	CY06	CY07	Mar-08	Dec-08	Mar-09
<i>Profit before tax</i>							
PSCBs	14.2	22.8	31.5	33.2	3.2	14.7	4.5
LPBs	31.0	60.5	85.6	69.7	24.5	74.5	19.8
FBs	7.2	11.6	6.3	2.5	0.8	0.4	0.6
CBs	52.4	94.9	123.5	105.4	28.5	89.6	24.9
SBs	(0.4)	(1.1)	0.1	1.7	(0.5)	3.9	1.3
All Banks	52.0	93.8	123.6	107.1	28.1	93.6	26.2
<i>Profit after tax</i>							
PSCBs	8.0	15.5	21.2	23.9	1.6	11.4	2.4
LPBs	21.8	41.1	59.1	47.4	16.4	49.5	12.3
FBs	5.8	8.0	4.3	1.2	0.3	(1.0)	0.2
CBs	35.6	64.6	84.6	72.4	18.4	59.9	14.9
SBs	(0.9)	(1.3)	(0.5)	0.9	(0.5)	3.3	0.9
All Banks	34.7	63.3	84.1	73.3	17.9	63.2	15.8

Table 3.2.2: Profitability Indicators

	Percent					
	CY04	CY05	CY06	CY07	Dec-08	Mar-09
Before Tax ROA						
PSCBs	2.4	3.3	4.0	3.6	1.4	1.7
LPBs	1.7	2.7	3.1	2.0	1.8	1.9
FBs	2.5	3.6	3.2	1.5	0.2	1.0
CBs	2.0	2.9	3.2	2.3	1.7	1.8
SBs	(0.4)	(1.0)	(1.3)	1.4	3.1	4.1
All Banks	1.9	2.8	3.1	2.2	1.7	1.8
Before Tax ROE (based on Equity plus Surplus on Revaluation)						
PSCBs	30.8	30.7	32.4	27.2	11.2	14.7
LPBs	28.8	40.1	36.2	20.4	18.3	18.1
FBs	26.7	38.9	30.0	13.5	1.6	6.7
CBs	29.0	37.2	34.7	21.9	15.9	16.8
SBs	0.0	0.0	0.0	0.0	-	-
All Banks	30.5	38.2	35.2	22.6	16.7	17.8

Figure 3.2.1: ROE Before Tax



Even in face of a number of constraining factors, the banking system registered profits during Mar-09 quarter. The system actually earned higher profit before tax of Rs26.2 billion compared with only Rs10.5 billion in Dec-08 quarter. The performance is however, below the corresponding quarter of CY08 (see Table 3.2.1). The earning indicators also observed a marginal improvement.

The profitability has been boosted by the continuous healthy earning posted by large banks. The high interest income for the quarter, which is better than the corresponding quarters of the previous years, underlies the improved earning performance. However, high loan loss charges and administrative expense partially offset the core income and moderated the profitability for the quarter.

Improved earning is shared by all categories of banks. The LPBs as usual remained the major contributor to the profitability of the system, while the PSCBs and the SBs⁵ improved their share in the overall profit of the system. The profit after tax (PAT) of the PSCBs increased by 50 percent compared with Mar-08, despite huge losses incurred by a PSCB. Similarly, PAT of the SBs increased to Rs1.3 billion against loss of Rs0.5 billion in corresponding quarter of the last year. The foreign banks which posted losses for CY08 were successful in restoring their profitability. Increase in interest and non-interest income along with administrative cost control measures helped them post profit before tax which is higher than the full year results of CY08 (See Table 3.2.1).

The better earning performance for the quarter has improved the before tax earnings ratios (see Table 3.2.2). The before-tax return on assets (ROA) increased by 10 bps to 1.8 percent, while Return on Equity (ROE) improved by 100 bps to 17.7 percent in Mar-09 (see

⁵ The profitability for two of the SBs namely Punjab Provincial Cooperative Bank and Industrial Development Bank of Pakistan represent results for nine months as they publish their annual account for July-June each year owing to the requirements laid down in their respective statutes.

Table 3.2.2 and Figure 3.2.1). However, due to higher tax charges, after tax indicators witnessed slight deterioration.

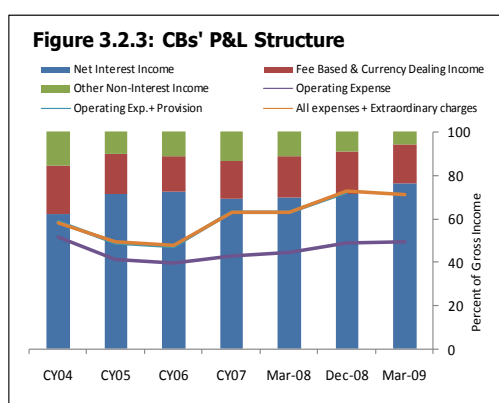
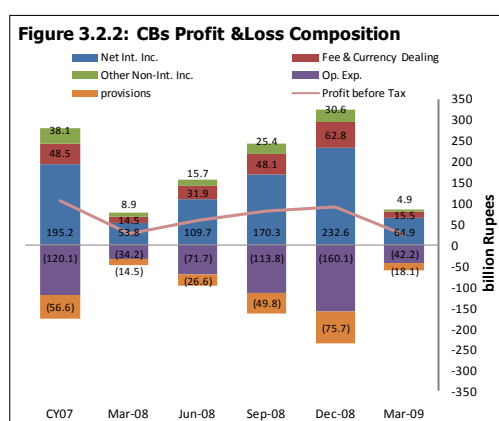
Groupwise, ROA and ROE improved for almost all categories of banks. The ROA for PSCBs improved by 30 bps to 1.7 percent while it improved by 80 bps to 1 percent for FBs. Similarly, the PSCBs and FBs ROE saw a substantial improvement in ROE. However, ROE for LBPs declined by 20 bps to 18.1 percent due to increase in equity base over the past two quarters.

The analysis of profit and loss composition for commercial banks shows a significant increase in net interest income over the quarter. As a result, their share in gross income increased by 5 percentage points to 76 percent. On the other hand, increase in non-interest income is relatively sluggish owing to decreasing dividend incomes. However, a healthy 50 percent growth in currency dealing income kept the non-interest income comparable with corresponding quarter of 2008 (see Figure 3.2.2).

Among the CBs, LPBs being the largest and active⁶ group increased its share in interest income by 4 percentage point to 83 percent while the PSCBs lost their share by equal proportion. Similar pattern is also observed for non-interest income (see Figure 3.2.3).

On the expense side, administrative expenses representing 50 percent of the gross income remain the major user of the earnings. The administrative expenses have remained high due to increase in salary expenses, increasing IT investments and expansion of branch network. Provisions which account for 21 percent of the gross income, is the second largest consumer of banks' earnings.

It would be important to highlight that system observed a massive increase in provisions charges during last quarter of 2008 due to loan loss charges and additional charges for



⁶ Some of the banks in PSCBs and SBs are under restructuring and are therefore not performing full-fledged banking function.

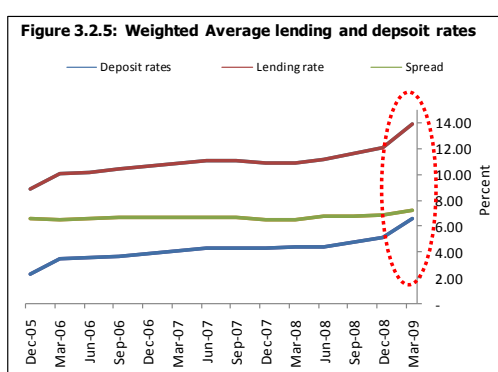
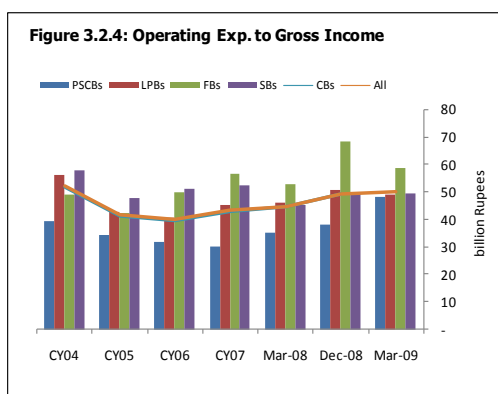


Table 3.2.3: Percentage Breakdown of Banking System's Total Assets (TA) by ROA

	CY05		CY06		CY07		Dec-08		Mar-09	
ROA	No. of Banks	Share in TA	No. of Banks	Share in TA	No. of Banks	Share in TA	No. of Banks	Share in TA	No. of Banks	Share in TA
0 and below	7	3.5	6	2.1	10	8.5	17	15.9	18	12.4
0 to 0.5	4	2.8	3	1.8	2	2.4	3	9.7	2	5.0
0.5 to 1	2	7	6	9.9	4	1.9	2	6.5	6	15.8
1.0 to 1.5	5	4	5	9.6	10	34.9	6	6.3	5	9.3
1.5 and Over	21	82.7	19	76.6	13	52.3	10	61.6	9	57.6

diminution in value of investments/shares. However, keeping in view the regulatory changes taking place across the globe, the regulators adjusted their regulations. Accordingly, SBP rationalized the provisioning requirements⁷ while SECP adjusted the disclosure requirements allowing the deferment of impairment losses on AFS securities over the current⁸ year. As a result of these changes, increase in loan loss provisions and the provision for diminution in value of investments somewhat diminished. The provisions increased by Rs18 billion against increase of Rs26 billion during Dec-08 quarter (Rs16 billion in corresponding quarter of the previous year). However, the provisions for the quarter consuming 21 percent of the gross income are still high (see Figure 3.2.4).

As a result of healthy increase in interest income, the cost to income ratio increased marginally by three quarters of a percentage point to 49.9 percent. The increase is even less for the commercial banking group. The change in ratio actually reflects the earning pattern as there is no significant change in pattern of expenses. The ratio has decreased for LPBs and FBs, while it increased both for PSCBs and SBs (see Figure 3.2.2 and Annex-I).

The analysis of core income show that net interest income increased despite decrease in advances by 5.6 percent during the year. The increase seems to have resulted from extraordinary increase in weighted average rate⁹; lending rates increased by 1.79 percentage points to 13.83 percent while deposit rates increase by 1.44 percentage points to 6.59 percent. This translates into increase in spread by 35 bps to 7.24 percent (see Figure 3.2.5).

⁷ See BSD Circular No. 2 dated January 27, 2009 on Amendments in PR-Provisioning for loans and advances.

⁸ See BSD Circular No. 4 dated February 13, 2009 on Revaluation surplus / (Deficit).

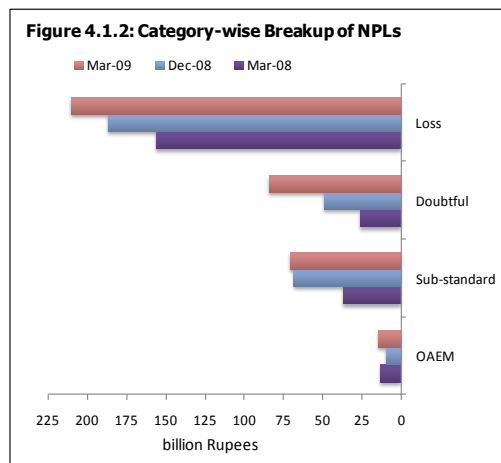
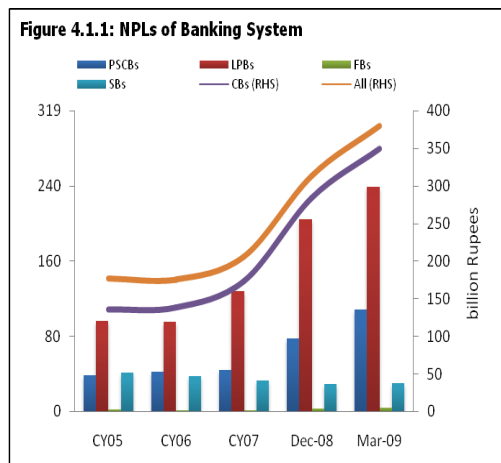
⁹ The weighted average rates are based on the data on mark-up/interest income and expense on advances and customer deposits respectively reported in the QRC for March, 2008. In the previous reports, data on interest rate published in monthly statistical bulletin had been used.

The earning capacity of the individual banks varied during the current quarter. The assets distribution on the basis of ROA shows that 14 banks, holding 66.9 percent market share, have ROA of one percent and above. As ROA of the banking system has declined, the number of banks with ROA below 1.0 percent increased to 26 from 22 whereas their share in total banking sector assets has increased by 1 percentage point to 33.1 percent during the quarter under review (see Table 3.2.3). The change in share structure indicate that some of the banks with higher assets base moved into higher ROA bracket, due to improved earnings, while others with smaller asset base receded to lower ROA bracket.

4. Risk Assessment of the Banking System

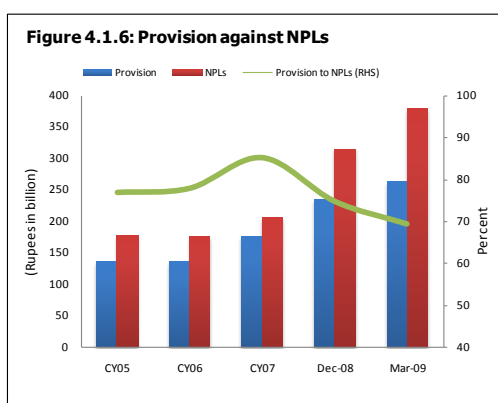
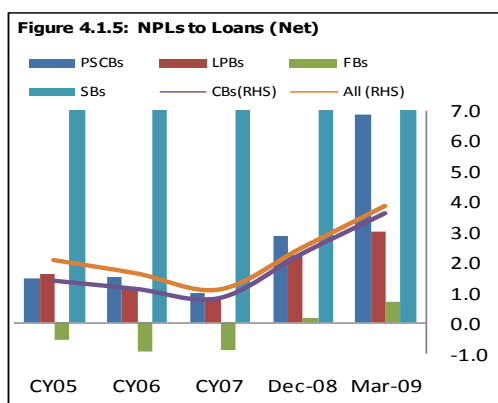
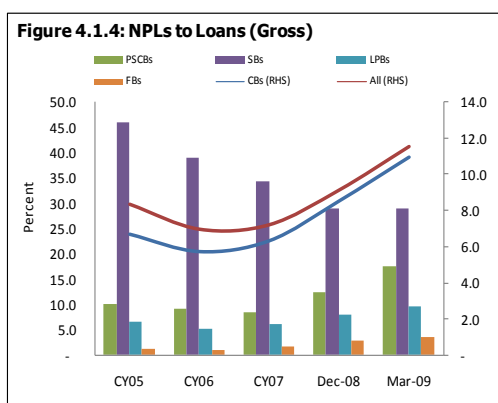
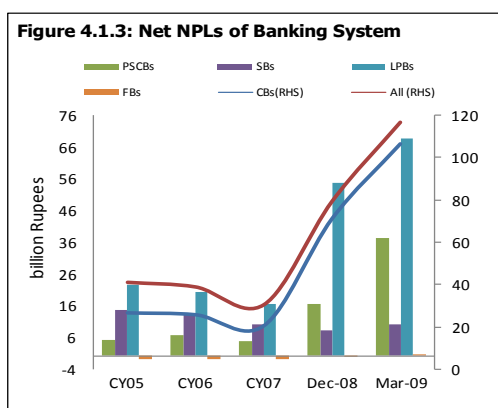
4.1 Credit Risk

The global economic slowdown, sagging economy and national insecurity are adversely affecting the business environment. As a result, banking sector saw a swift increase in NPLs during the last two quarters, signifying substantial increase in credit risk. The NPLs to loan ratio increase by 2.4 percentage points to 11.5 percent. The souring credit conditions have accelerated this increase; while slowdown in economic activities led to 4.4 percent decline in gross advances.



The infected portfolio of the banking system increased by 21 percent to Rs 379 billion during the quarter. Increase in NPLs is observed in almost all banks; however, substantial increase took place in middle tier and small sized banks. In some cases increase in NPLs is higher than decrease in advances. PSCBs and LPBs contributed most of the increase in NPLs of the system; 46 percent increase in NPLs of the former and 53 percent in latter group. Particularly, NPLs of PSCBs increased by Rs30 billion representing 40 percent surge over the previous quarter. Further analysis show that NPLs of a PSCB, after remaining stagnant for last two quarters, more than doubled over the Mar-09 quarter, indicating recognition of some pending weak quality advances. This sudden increase caused sharp spike in NPLs of the group as well as the banking sector (see Figure 4.1.1).

Categorical analysis of NPLs shows an increase across all classifications. A significant increase of Rs 35 billion took place in doubtful category, which represents influx of most of the fresh NPLs. The LPBs and PSCBs are again the main source of increase. Another discouraging development is further increase in the initial categories of NPLs (OAEM, substandard and doubtful) that require partial provisioning coverage. NPLs in these first three categories increased to 45 percent from 32 percent a year



earlier. This trend indicates that in periods ahead, banks might have to provide additional loans losses and face constrained earnings (see Figure 4.1.2).

Growing NPLs translated into a noticeable addition in Net NPLs (see Figure 4.1.3). The net NPLs saw a 47 percent increase over the quarter. Continuous flow of NPLs in classification categories requiring partial provisions in addition to adjustments in provisioning requirements during the current quarter contributed in the increase of net NPLs. Though LPBs have major share in net NPLs however major increase took place in PSCBs; like NPLs, their net NPLs also more than doubled.

Increasing NPLs along with declining advances further deteriorated the infections ratios. NPLs to Loan ratio of the banking system increased sharply from 9.1 percent in Dec-08 to 11.5 in Mar-09. The trend analysis of the ratio shows that after bottoming out to 6.9 percent in 2006, the ratio later on moderately increased to 7.2 percent in 2007. The upsurge in ratio picked up in the next four quarters of 2008, when it increased by 1.9 percentage points. The infection ratio of individual market players witnessed mixed trend during the last three years – some of the banks experiencing deterioration while others improvement. The ratio worsened for all the banks during Mar-09 quarter, with more pronounced increase in a public sector bank and some small sized banks. It saw a 5.2 percentage points' increase for the PSCBs, followed by a 1.8 percentage point increase for LPBs (see Figure 4.1.4).

The NPLs to loans ratio (net) which declined to around 1 percent by the end of 2007, reached 2.5 percent during 2008 and increased to 3.9 during the quarter under review – on the pattern of gross infection ratio (see Figure 4.1.5).

The soaring NPLs enhanced the provisioning requirements. The provisions increased by Rs28.3 billion which fell short of increase in NPLs of Rs65 billion. As a result, the NPLs

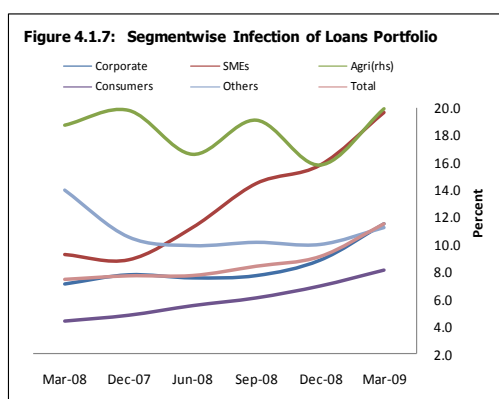


Table 4.1.1: Segmentwise Infection of Loans Portfolio

Sector	In percent		Share in total loans (%)
	Dec-08	Mar-09	
Corporate	8.9	11.5	62.7
SMEs	15.8	19.6	10.9
Agriculture	15.8	19.9	4.6
Consumers	6.9	8.1	10.5
Credit Cards	5.5	7.0	1.2
Auto Loans	5.9	6.2	2.7
Consumer Durables	7.8	10.2	0.0
Mortgage Loans	7.4	9.0	2.4
Others	7.8	9.1	4.2
Commodity Finance	1.4	1.5	6.8
Staff Loans	1.0	1.1	2.0
Others	10.0	11.3	2.3
Total	9.1	11.5	100.0

coverage ratio declined to 69 percent from 74.7 percent in Dec08 (see Figure 4.1.6). The provisions to NPLs improved to 85 percent in 2007 after strengthening of provisioning requirements. However, with the increase in NPLs especially in the partial provision categories and rationalization of provisions requirements in January, 2009, the coverage ratio further declined in Mar-09 quarter (figure 4.1.6). Deterioration in asset quality is also observable in Capital impairment ratio (Net NPLs to capital) which increased to 19.6 percent in Mar-09 from 13.6 percent in Dec-08.

Like overall NPLs trend, infection ratio increased for all the segments (see Table 4.1.1). The infection ratio of corporate sector, with highest exposure in overall portfolios, displays a 71 percent increase in NPLs. The Corporate, SME and Agriculture which represent 78 percent of the overall loan portfolio, are responsible for 94 percent increase in infected portfolio. An interesting trend is observed in Agriculture sector NPLs ratio; where infection ratio variation is around 5 percent over each quarter, indicative of the seasonal pattern. Agri-NPLs increase during sowing season, while decrease in harvest season. NPLs of the SME sector continue to rise at relatively fast pace (see Figure 4.1.7). Analysis of NPLs by the end use of loans shows that infection is more pronounced in working capital finance, where they increased by 28 percent over the quarter, indicating slackness in turnover of inventories and receivables, in the wake of general slowdown in business activities.

Table 4.1.2: Sectorwise Infection of Loans Portfolio

Sectors	Dec-08		Mar-09		Share in	
	NPLs to loans		NPLs		Loans	
Textile	14.6	17.9	29.9	19.3		
Elec.& transmission of energy	3.4	6.5	5.5	9.6		
Agribusiness	8.9	11.6	4.5	4.5		
Chemical & Pharmaceuticals	7.7	7.8	2.3	3.4		
Cement	6.6	9.2	2.1	2.6		
Sugar	9.1	9.6	2.2	2.6		
Auto & Transportation	7.5	14.3	2.7	2.2		
Financial	5.4	8.7	1.1	1.4		
Shoes & Leather garments	8.6	8.7	0.5	0.7		
Insurance	0.0	0.6	0.0	0.1		
Individuals	8.7	9.5	11.6	14.2		
Others	8.6	11.0	37.5	39.3		
Total	9.1	11.5	100.0	100.0		

Infection ratio of consumer finance increased with decreasing lending portfolio and increasing NPLs. The infection ratio of consumer finance portfolio increased by 1.2 percentage points to 8.1 over the quarter.

Sector analysis of asset quality confirms the changes taking place in the overall portfolio structure and infection rate (see Table 4.1.2). Among various sectors, NPLs of textile, cement, agribusiness, automobiles & transportation and Electronics & Transmission of Energy increased quite substantially. Most of infected portfolio in

Table 4.1.3: Credit shocks-Descriptions

C-1	15% of performing loans moving to substandard, 15% of substandard to doubtful, 25% doubtful to
C-2	Tightening of loan classification i.e. all NPLs under OAEM require 25% provisioning, all NPLs under substandard require 50% and all NPLs in doubtful category require 100% provisioning.
C-3	Deterioration of loans to the textile sector (25%) directly downgraded to doubtful category
C-4	25% of consumer loans (auto loans, personal loans & consumer durables only) classified into doubtful
C-5	Default of three largest exposures (Fund Based

cement and electronic sector are concentrated among a few defaulting borrowers. The textile sector due to its major share in loan portfolio provided largest increase in the infected portfolio. Keeping in view the present economic circumstances banks are facilitating the promising businesses through rescheduling/restructuring of loans; Textile, Electronic & Energy Transmission and Cement have been the major beneficiary.

In order to assess the resilience of the banking system to adverse movements in credit risk factors, lending portfolio has been stress tested for five different types of shocks (see Table 4.1.3).

Table 4.1.4: Credit shocks

Shock	Impact of shocks	
	% point change in CARafter Shock	Adjusted CAR after shock
Credit Shock C-1	(2.19)	10.7
Credit Shock C-2	(1.36)	11.6
Credit Shock C-3	(1.71)	11.2
Credit Shock C-4	(0.71)	12.2
Credit Shock C-5	(7.37)	5.5

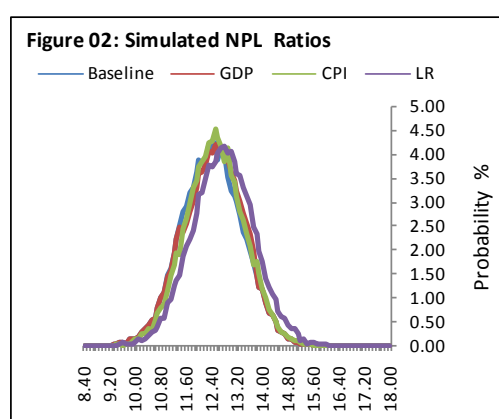
The credit shock C-1 leads to reduction in the CAR of the system by 2.19 percentage points to 10.7 percent (See Table 4.1.4). Similarly, by tightening the provisions under shock C-2, the overall CAR of the banks faces a reduction of 1.36 percent points to 11.6 percent. The textile sector specific shock C-3 leads to decline in the CAR of the banking system by 1.71 percentage points. Under stress C-4, the CAR of banks marginally declined by 0.71 percentage points. The impact of concentration risk shock C-5 is the largest on the CAR. The CAR of banking sector would decline by 7.4 percentage points to 5.5 percent (see Table 4.1.3).

The overall results of stress shock on the banking system show sufficient resilience of the banking system except for concentration risk. Given the slowdown in economy and business environment, banks need to rationalize their concentration profile and strengthen the vigilance of their large exposures. The results of the macro stress testing show a potential for further increase in credit risk in the quarter ahead in face of the adverse movements in financial as well as economic factors (see Special Section: Macro-stress Testing of Credit Risk).

Special Section 1: Macroeconomic Stress Testing of Credit Risk

Table 01: Stress Testing Simulation Results (% NPL)

	Baseline	Stressed Scenarios		
		CPI	GDP	LR
Average	12.482	12.505	12.612	12.687
90 P	13.975	13.98	13.985	14.051
95 P	14.284	14.286	14.363	14.546
99 P	14.883	14.895	14.92	15.059
99.5 P	15.077	15.083	15.102	15.158
99.9 P	15.362	15.399	15.415	15.873

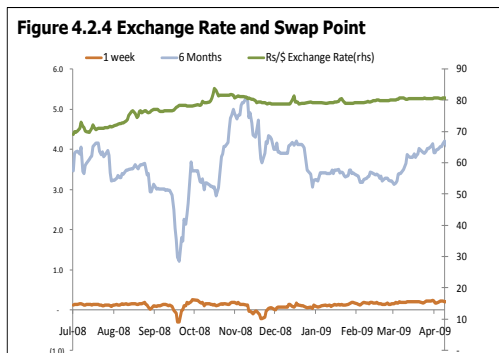
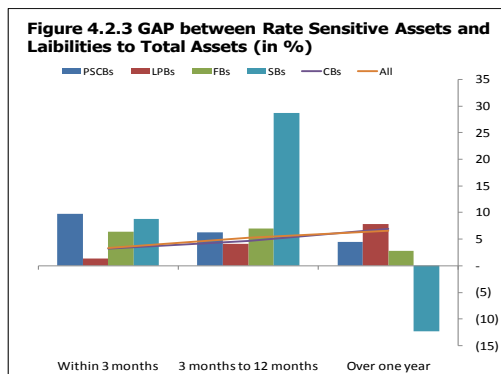
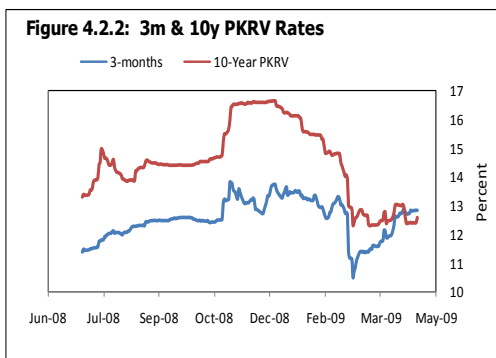
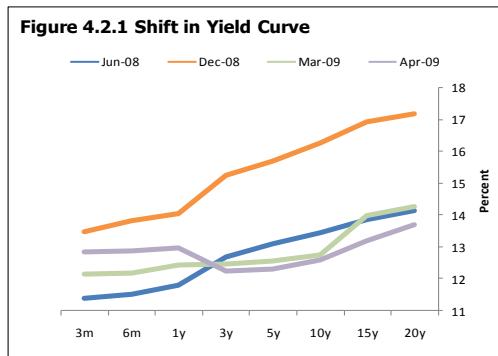


The macroeconomic stress testing considers the risks faced by the banks to be highly dependent upon the macroeconomic environment. In case of stress testing the credit risk of the banks, the Credit Portfolio View (CPV) methodology¹⁰ is used to (a) forecast the NPL ratio of one future quarter, (in this case, future quarter is Jun-09) and (b) to construct Monte Carlo simulation to stress test various scenarios. The present exercise considers NPL to loan Ratio (NPLR) of all commercial banks which increased from 9.1 percent in Dec-08 to 11.54 percent in Mar-09.

Macro stress testing for Credit risk show that under base line scenario, the CPV methodology forecast NPL at 12.48 percent of loans for the period Jun-09 (See Table 01). The estimates show a 98 bps increase in infection ratio over the current infection ratio of 11.54 percent. Under stressed scenarios for various macroeconomic variables, average NPLs to loan ratio is estimated to increase to 12.69 percent or above for the lending rate (LR) stress scenario. Review of the tail events show that there is 0.1 percent probability that the NPL ratio may worse-off to 15.87 percent or above in case of extreme lending rates (LR) shock.

¹⁰ For the detailed CPV methodology, see Quarterly Performance Review – December 2008.

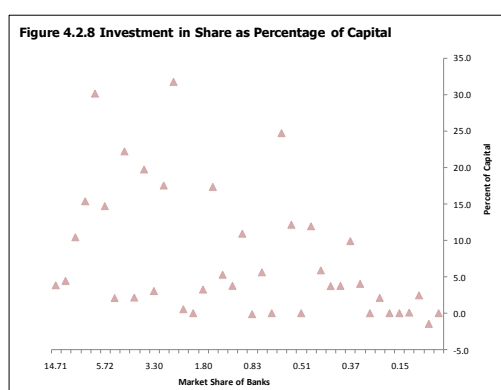
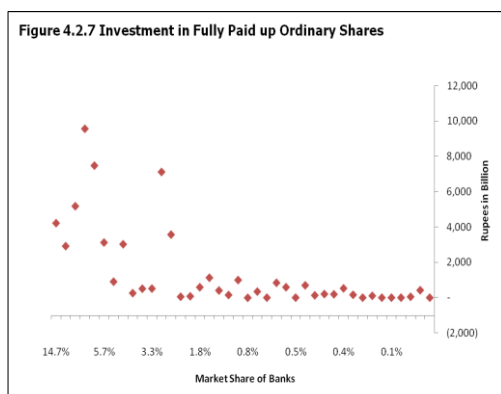
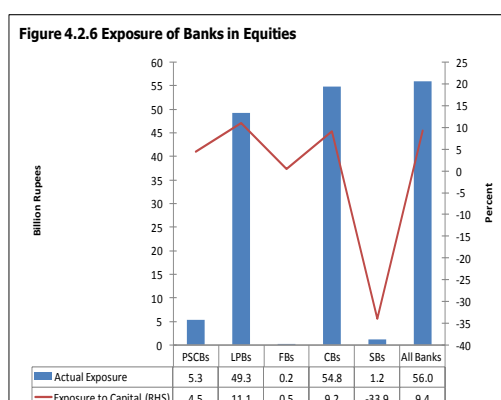
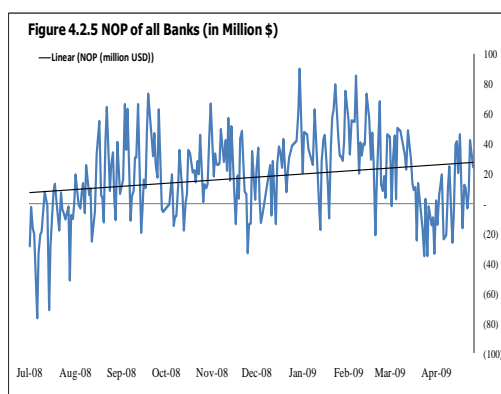
4.2 Market Risk



Market Risk profile of the banking system is dominated by Interest Rate risk that remained somewhat subdued during the quarter under review. With easing out of the liquidity stress, the yield curve started shifting downwards and reached around the level of Jun-08 by the end of Mar-09. The yield curve after getting flattened in short term during Mar-09 quarter got inverted by Apr-09, depicting market expectations for easing out of interest rates (see Figure 4.2.1). Likewise, the PKRV interest rate for 3m came down further from 13.5 percent in Dec-08 to 12.8 percent in Mar-09 and afterwards witnessed slight inch up and the spread between the short term and long-term PKRV rates contracted significantly (see Figure 4.2.2).

The changes in term structure of interest rate influence the interest rate risk a great deal if there is substantial re-pricing GAPS. The GAP position of banks shows that for the time buckets of upto 3 months, 3 to 12 months and over 1 year buckets, re-pricing GAPS were generally within acceptable ranges i.e. ± 10 percent of the total assets. GAPS in almost all the time buckets stayed in positive range except for Specialized Banks as one of the banks in this category has large negative equity, which is covered through rate sensitive liabilities (see Figure 4.2.3).

On the Exchange Rate risk front, there was depreciation in real exchange rate since Dec-08 (see Figure 4.2.4). The announcement of IMF package kept the USD/PKR exchange rate sustainable and PKR stood at Rs80.5 for a dollar as on March 31, 2009. In post quarter weeks rupee-dollar parity stays close to Rs80.6. As banks' net open position largely remained positive during the quarter, there had been an overall positive effect on the earnings of the banks and the exchange rate exposure of banks remained subdued (see Figure 4.2.5). The stress test results also endorse the fact that



changes in exchange rates will have marginal impact on the solvency of banks.

Equity price risk of a bank is primarily driven by its exposure in the equity market. During the quarter under review, capital market recovered significantly, thus enlivening the investor confidence. Accordingly, equity exposure of the banking system (including investments in fully paid up shares both in listed and unlisted stocks but excluding the subsidiaries and associates) increased to Rs56.0 billion by the end of Mar-09 (see Figure 4.2.6). Investments in terms of banks' equity (net worth) also recovered to 9.4 percent after experiencing decline in Dec-08 (7.9 percent) and Sep-08 quarters (8.1 percent). Group wise, LPBs continued to dominate the equity exposure with equity investment of Rs49.3 billion, followed by PSCBs with Rs5.3 billion exposure.

Disaggregated analysis indicates that top 5 banks (holding around 52 percent of the total banking assets), also hold 52 percent of the total equity investments (see Figure 4.2.7). Further 23 out of 40 banks have exposures of less than 5 percent in terms of their equity (see Figure 4.2.8). With only 7 banks having equity exposures of more than 15 percent, the exposure of the banking sector remains in comfortable range.

To examine the resilience of the banking system to changes in the Market Risk profile, it has been stressed for eight different kinds of shock (see Table 4.2.1). The stress test results for the Market Risk show that banks have strong capacity to withstand the adverse movements in market risk factors.

Increase in interest rates by 500 bps under shock IR-1 would reduce the CAR of the banks by 2.0 percentage points to 10.9 percent. Similarly, the shift in yield curve under shock IR-2 would impact the CAR of the banks by 0.8 percentage points to 12.1 percent.

The exchange rates shocks ER-1 would reduce the CAR of banks by 0.05 percentage points. However, in shock ER-2, the CAR of the banks increases by 0.05 percent, indicating that banks

Table 4.2.1: Stress Tests - Market Risk

Interest Rate Shock	
IR-1	Increase in interest rates by 500 basis points
IR-2	Shift coupled with flattening of the yield curve by increasing 500, 300 and 200 basis points in the three maturities respectively
Exchange Rate Shock	
ER-1	Depreciation of currency exchange rate by 25%
ER-2	Appreciation of currency exchange rate by 25%
ER-3	Depreciation of PRs against all currencies (25%) and deterioration of un-hedged FX loans
Equity Price Shock	
EQ-1	Fall in the equity prices by 50%.
EQ-2	Fall in the equity prices by 60%.
EQ-3	Fall in the equity prices by 70%.

Table 4.2.2: Impact of Shocks

Shock	% point change in CAR after Shock	Adjusted CAR after Shock
IR-1	-2.02	10.9
IR-2	-0.85	12.9
ER-1	-0.05	12.9
ER-2	0.05	13.0
ER-3	-0.30	12.6
EQ-1	-0.53	12.4
EQ-2	-0.62	12.3
EQ-3	-0.71	12.2

are holding foreign currency denominated liabilities slightly higher than foreign currency assets. However under the combined exchange rate and credit risk shock ER-3 the CAR of the banks reduces by 0.30 percentage points to 12.6 percent (see Table 4.2.2).

Different equity price shocks will be having maximum impact of around a percentage point on the CAR. Under the equity price shocks EQ-1, EQ-2 and EQ-3 the CAR of the banks falls by 0.53, 0.62 and 0.71 percentage points, respectively.

The stressed CAR of the system at 12.2 percent, after 70 percent decrease in the equity prices, signify that banking sector is safely placed to absorb such type of extreme shocks.

4.3 Liquidity Risk

The liquidity situation has been gradually easing out since the liquidity shortage in the second half of 2008. As the deposit has registered significant increase since then, the deposit to M2 ratio has improved. However, during the quarter under review, deposit base remained stable, and its share in M2 remained more or less intact at Dec-08 levels (see Figure 4.3.1).

During the quarter, fund based liquidity of the system improved due to change in asset structure (see section: Assets and Funding Structure) in favour of investment in marketable govt. papers. Accordingly, the key liquidity indicators viz. ADR (ERF adjusted) came further down to 67.5 percent and liquid assets' share in total assets improved to 30.5 percent (see Figure 4.3.2). Further, the regulatory liquidity reserve maintained by banks gradually improved to 37.1 percent by end of April, 2009 (see Figure 4.3.3). Liquidity profiles of individual banks also further improved during Mar-09 quarter. At end of the quarter under review, only one bank was non-compliant with CRR and another with SLR.

The Government securities especially the short-term govt. papers (MTBs) in different investment categories represent the fund-based liquidity available within the banking system. The MTB holdings have increased by 19.4 percent in Mar-09, mainly in HTM and AFS categories. MTBs in the AFS category increased by 2 percentage point to 93 percent (see Figure 4.3.4), while HFT category decreased by 2 percentage point to reach 3 percent. The share of HTM remained at 4 percent for this quarter.

Monitoring the market's liquidity position on regular basis, SBP adjusts its injections and mop-ups of liquidity through open market operations (OMOs). During most part of the quarter SBP was gradually mopping up the liquidity that had been consciously left in the market to address the effects of liquidity pressure in October 2008. However, since late

Figure 4.3.1 Deposit to M2 Ratio

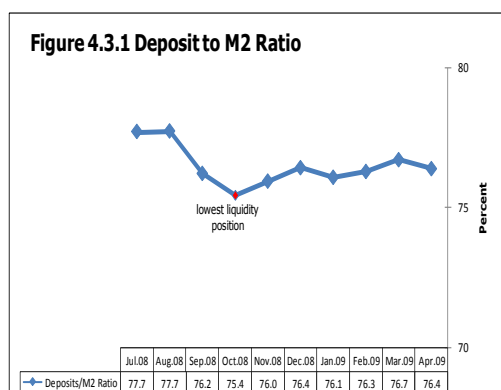


Figure 4.3.2 Liquidity Indicators

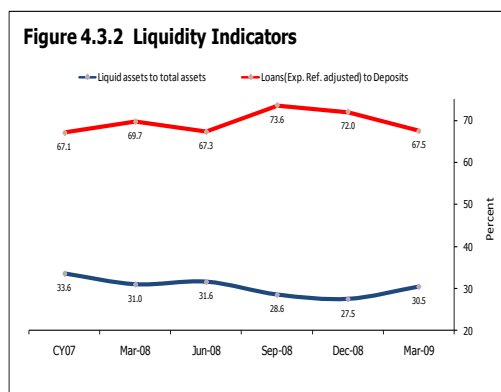


Figure 4.3.3 Maintained & Required Liquidity of TDL (in %)

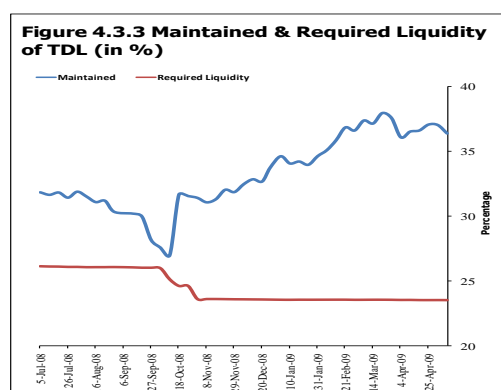
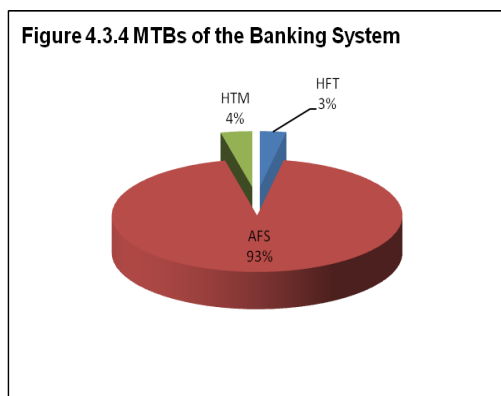
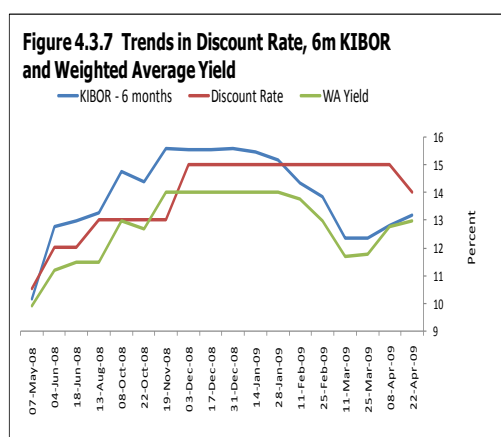
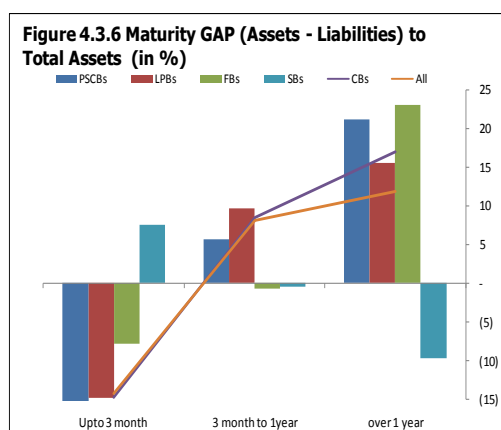
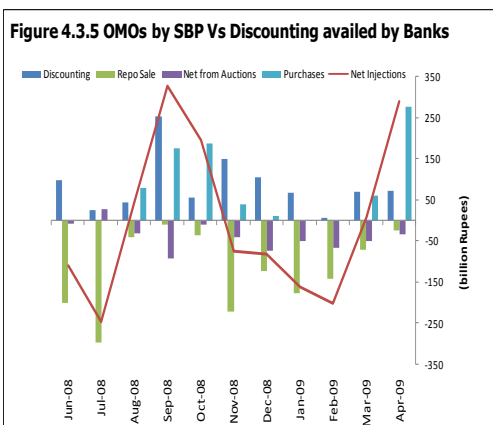


Figure 4.3.4 MTBs of the Banking System





Mar-09 to end of Apr-09, SBP injected around Rs290 billion on net basis (see Figure 4.3.5).

Although the effects of the volatile liquidity situation during the previous two quarters have largely eased off, GAPs between the maturity of assets and liabilities are still relatively higher. Group wise analysis indicates that PSCB, FBs and SBs were carrying significant gaps of more than ten percentages of total assets in different maturity buckets. LPBs, which have been exhibiting good liquidity management for the last two quarters, suffered this time around as they carried gaps in upto 3 months and over 1 year time buckets. Consequently, the GAP position for all banks has gone beyond the limit of +10 percent in upto 3 months and Over 1 year buckets (see Figure 4.3.6).

As mentioned in the last review, there has been considerable liquidity in the banking system and as a result, KIBOR has been experiencing a declining trend during the quarter (see Figure 4.3.7). SBP announced reduction in the discount rate by 100 bps on April 20, 2009, bringing it down to 14 percent. Since then, interbank lending rates have increased in the following weeks due to increased credit demand for commodity operations. Moreover, this phenomenon highlights the gradual normalization of market and the tendency on the part of interbank lending rates to rationalize vis-à-vis discount rate. Further, banks have been opting cautious lending approach, owing to the economic slowdown and heightened credit risk.

The stress tests results of Pakistani banks continued to remain reasonable for the quarter ending Mar-09. Liquidity of the banks is assessed by calculating net cash flows (cash inflows minus cash outflows) of banks after assuming certain level of daily deposit withdrawals and generating cash inflows by converting 80 percent of liquid assets and one percent of non-liquid assets into cash. This shock assumes withdrawal of customer deposits by 2 percent, 5 percent, 10 percent, 10 percent and 10 percent for five consecutive days, respectively. (see Table 4.3.1).

Table 4.3.1: Liquidity Shock		Number of Banks becoming Illiquid after Shock		
		3 days	4 days	5 days
L-1	Withdrawal of customer deposits by 2%, 5%, 10%, 10% and 10% for five consecutive days respectively.	1	3	6

The results show that none of the banks becomes illiquid after two days of withdrawal. However, after three days of the consecutive withdrawal, only 1 bank would become illiquid. However, after the consecutive 5 days withdrawal of deposits, 6 banks would become illiquid.

4.4 Operational Risk

Keeping in view the current global financial turbulence, increased volatility and the increased frequency of unforeseen incidents, the importance of operational risk framework has increased many folds. Although the scope of operational risk is vast and diversified, some of the major issues related to operational risk that banks face are:

1. People risk – Lack of awareness / proper training programs / non-following of policies & procedural manuals
2. System risk – Heavy reliance on systems, system down time, minor / major bugs, miscalculations etc.
3. Internal / external events – Fire incidents, political disruptions, earthquakes, floods etc.
4. Fraud & forgeries

Proper management of operational risk improves the quality and firmness of earnings of financial institutions by ensuring stable cash flows, aiding in their survival. On the other hand, the increasing change in the technological advancements has called for proactive approaches for operational risk management. The risk exposure generally arises from highly automated technologies, complex products, e-banking and mergers/acquisitions in the banking system.

Apart from the implementation of Basel II which requires dedicated capital cushion for covering operational risk, State Bank of Pakistan has been advising banks to develop a sustainable operational risk management framework to have better and sound banking operations. The guidelines from SBP generally address:

1. Establishment of adequate control and risk management framework that is commensurate with the size and nature of bank's operations and risks.
2. Formulation of Business Continuity Plan for catering to any sudden and significant disruption in the business environment.
3. IT Security Management:

- a) deployment and review of immaculate IT security measures
 - b) review of IT security controls for impeccable processing of information
4. Identifying and bridging the gaps in operational risk policy & procedure and ensuring strict compliance
 5. Periodical review / update of AML/KYC plans
 6. Examination of physical controls and of guidelines including detail of various insurance policies in place.

Table 4.4.1 Break-up of Fraud and Forgeries - as on December 31, 2008

(Rs. in million)		
Category	No. of cases	Amount Outstanding
Serious frauds (more than Rs. 10 million)	186	4,017
Medium severity cases	399	1,112
Low severity cases	5,753	1,426
Total	6,338	6,555

Criteria for Fraud and Forgeries Categories

Serious Frauds	More than 10
Medium severity Cases	1 to 10
Low Severity Cases	Less than 1

**Table 4.4.2 Break-up of Fraud and Forgeries
Detected during the quarter December 31, 2008**

(Rupees in million)		
Category	No. of cases	Amount Involved
Serious frauds (more than Rs. 10 million)	13	687
Medium severity cases	33	126
Low severity cases	743	75
Total	789	888

Apart from ensuring the sound systems and practices in the management of operational risk, SBP monitors the magnitude and trends of the risk emanating from the failures in control environment and system of banks¹¹.

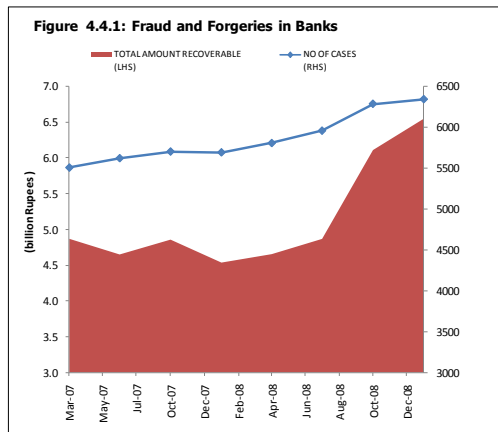
Aggregate analysis of cases of Fraud and Forgeries shows that during Oct-Dec 2008 quarter total outstanding cases have marginally increased by 0.8 percent to 6,338 (6,288 in Sep-08), whereas amount outstanding against these case increased by 7.2 percent to Rs6.5 billion. Detailed study reveals that number of cases for Serious-Fraud and Low-Severity categories increased by 1.1 percent each whereas Medium-Severity cases declined by 2.9 percent. Outstanding amount, for Low Severity cases increased by 83.1 percent to Rs1.43 billion from Rs0.78 billion.

A quick comparison of the fraud & forgery cases detected during the quarter Dec-08 reveals that there has been 38.7 percent increase in Fraud and Forgeries cases as compared to cases detected during Sep-08 quarter. Serious Fraud cases represented 1.6 percent of the total incidents reported with outstanding amount representing around 77 percent of the total outstanding amount (see Table 4.4.2). The number of Low Severity Cases contributed around 94.2 percent of the total cases and 8 percent in terms of total amount involved. Under Medium Severity category, 33 cases were

¹¹ See BSD Circular No. 01 of 2005 on Reporting Requirements on Frauds/Forgeries/Dacoities.

reported during Dec-08 quarter as compared to 54 cases reported during Sep-08 quarter.

Although the amount involved in fraud and forgery cases is hovering around Rs5.6 billion, the number of fraud / forgery cases is on the rise for last one year or so. This increasing trend is a source of concern for banking industry as well as SBP (see Figure 4.4.1). Banks need to be more proactive in their approach to reduce the numbers of such cases.



For other financial risks categories such as market and credit risk, plenty of sophisticated economic models are available for quantifying exposure of risks. However, quantification of operational risk is still a relatively new field. Although banks are in the process of establishing operational risk management frameworks, the overall progress in developing objective models still has a long way to go.

It is imperative for banks to devise systems to ascertain true quantum of operational risk according to their size, sophistication, nature and complexity of operations. SBP is working closely with Pakistan Bankers Association (PBA) and other stakeholders so as to provide a conducive regulatory environment for banks to come up with sound strategies, strong internal controls and effective reporting for minimizing operational risk event and resultant losses¹².

Collection of data on loss events and potential losses is critical; therefore banks/ DFIs are encouraged to collect data on the following dimensions;

1. Gather actual loss events
2. Risk Identification & Assessment

Another important area in measurement of operational risk is developing the Key Risk Indicators for different business lines and events. KRIs are one of the most common ways of measuring actual values of risk causes, risk events and their consequences. Identification and development of KRI is an ongoing process as it measures and anticipates inadequacies in

Effectiveness	Comparability	Ease of Use
<p>Indicators should:</p> <ul style="list-style-type: none"> • Apply to at least one specific risk and one business function or activity. • Be measurable at specific points in time; • Reflect objective measurement rather than subjective judgment; • Track at least one aspect of loss profile or event history, such as frequency, average severity, cumulative loss or near-miss rates; and • Provide useful management information 	<p>Indicators should:</p> <ul style="list-style-type: none"> • Be quantified as an amount, a percentage, or a ratio; • Be a reasonably precise and definite quantity; • Have values that are comparable over time; • Be comparable internally across businesses; • Be reported with primary values and be meaningful without interpretation to some more subjective measure; • Be auditable; and • Be identified as comparable across organizations (if in fact they are) 	<p>Indicators should:</p> <ul style="list-style-type: none"> • Be available reliably on a timely basis; • Be cost-effective to collect; and • Be readily understood and communicated

¹² See BSD circular No. 3 of 2007 on Minimum Requirements for formulation of Operational Risk policy.

process and control activities. Operational risk management and measurement depends largely on quality of KRIs. Therefore, it is essential that identified KRIs must fulfill the criteria for good KRIs (see Table 4.4.3). Each business line may have its specific set of indicators, but how will a firm determine if a specific indicator is useful. It is important that KRIs are more specifically transactions related.

The measurement of capital requirement has been evolving. It is estimated that banking system, which mainly follows the Basic Indicator Approach for calculating capital charge under Basel-II framework, is maintaining capital of around Rs40 billion (12 percent of the overall risk-based capital requirements) for covering operational risk. In addition to this, banks are required to formulate and strengthen sound Risk Control and Self Assessment (RSCA) systems, with a special focus on capacity building.

5. Performance of Islamic Banking

After showing a strong growth since its inception in 2002, the Islamic banking industry in Pakistan witnessed the impact of slowdown in overall economy. Total asset of the industry grew at a low rate of 0.7 percent (to Rs278 billion) lower than banking sector growth rate of 1.6 percent. Right from its commencement, Islamic banking has expanded at a significantly greater pace than the overall banking system. Over these years, the industry grew at an average annual rate of 37 percent, increasing its market share to 4.9 percent by Dec-08. However, due to slightly slower growth during the quarter, the share has slightly receded to 4.8 percent. Similarly, outreach of Islamic Banking also expanded passively during the quarter. The branch network grew by 1.6 percent to 521 branches by the end of the quarter, compared with 514 branches at the end of Dec-08 and 291 in Dec-07 (see Table 5.1).

Analysis of the sources and uses of funds shows gradual increase in the share of deposits, which dominate the funding structure of the Islamic banking while financing remains the major end use of Islamic Banking funds. The deposits of Islamic banking grew at 2.3 percent to Rs206.2 billion during the quarter (Rs201.7 billion in Dec-08) increasing their share in overall funding structure to 74.1 percent from 73.0 percent in Dec-08 (see Figure 5.1).

Financing of IB witnessed an over the quarter sharp decline of 5.9 percent to Rs136.2 billion. Share of financing in overall composition of assets declined to 48.9 percent (52.2 percent in Dec-08). This share was taken up by investments and interbank balances & placements. The investment registered a strong growth of 16.1 percent to Rs49.0 billion. Resultantly, their share in asset base increased to 17.6 percent (15.3 percent in Dec-08), while Cash, Bank Balances and placements constitute

Table 5.1: Islamic Banking Participants

	CY02	CY04	CY06	CY07	Mar-08	Dec-08	Mar-09
No. of Islamic Banks (IBs)	1	2	4	6	6	6	6
No. of Branches	6	23	93	186	210	384	386*
No. of conventional banks operating Islamic Banking Branches	-	7	12	12	12	12	12
No. of Islamic Banking Branches (IBBs)	-	21	57	103	103	130	135*

* These numbers also include Sub Branches.

Figure 5.1: Composition of Liabilities

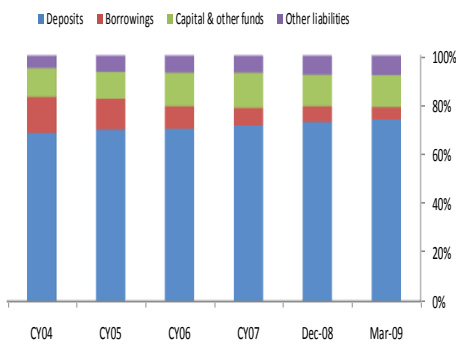
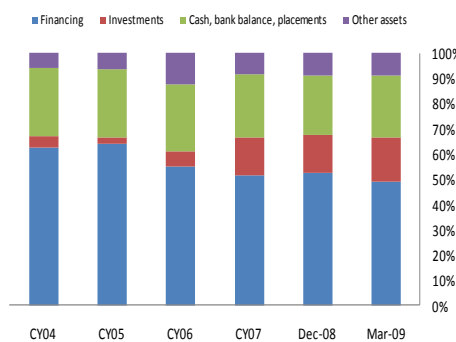


Figure 5.2: Composition of Assets



23.3 percent of the total assets (see Figure 5.2).

High share of cash and balances gives the adequate liquidity, which has been essential for coping with such stresses as was experienced by the banking industry during last quarter. However, this phenomenon itself reflects upon the limited investment alternatives available to Islamic banking, which affects the operating efficiency of these institutions. SBP, in collaboration with Government of Pakistan is gradually resolving the issue; it has conducted three auctions of GoP Ijara Sukuk¹³ of 3 years maturity amounting to Rs27.8 billion. Investment in sukuk has enhanced the share of Government bonds in the overall investment portfolio of Islamic banking, providing stabilization to earnings.

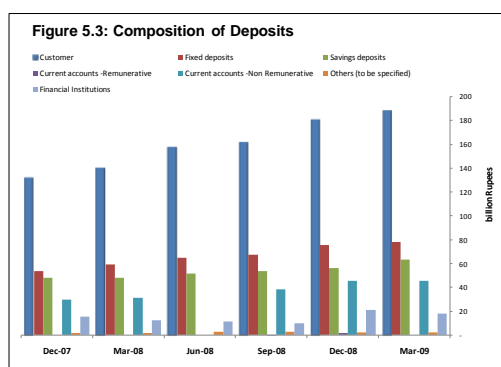
Table 5.2: Key Performance Indicators

Indicator	Percent						
	CY04	CY05	CY06	CY07	Mar-08	Dec-08	Mar-09
NPFs to total financing	0.9	1.0	1.3	1.2	1.5	2.3	4.5
Net NPFs to net financing	0.2	0.2	0.4	(0.1)	0.2	0.8	2.3
Provision to NPFs	82.3	80.6	72.0	108.7	84.2	67.6	50.6
Net Markup Income to total assets	1.4	2.3	2.4	2.9	4.1	4.5	1.3
Non Markup Income to total assets	1.4	1.7	0.9	1.2	1.0	0.9	0.2
Operating Expense to Gross Income	65.3	49.9	72.8	70.0	74.3	76.0	66.0
ROA (average assets)	1.2	1.7	0.9	0.9	0.8	0.8	0.8
Growth in Assets	241.8	62.0	66.9	72.9	3.0	10.1	0.7
Growth in Deposits	259.5	65.4	67.7	76.0	3.5	17.7	2.3
Growth in Financing	218.2	66.3	43.3	62.1	12.5	1.8	(5.9)

In line with increase in credit risk of the banking system, the asset quality indicators of the IB also came under significant stress. NPFs experienced an unprecedented over-the-quarter increase of 83 percent to Rs 6.3 billion. Due to decline in financing, the infection ratio deteriorated even more sharply to 4.5 percent (2.3 percent in Dec-08). Since major share of this increase in NPFs was contributed by Doubtful and Substandard categories which require partial coverage, NPF coverage ratio also came off significantly to 50.6 percent (67.6 percent in Dec-08). As a result, net infection ratio also increased by almost three times to 2.3 percent. Owing to low NPFs to financing ratio, Islamic banking till the end of CY07 had a NPF coverage ratio of more than 100 percent. However, with the addition of fresh NPFs that were mainly in Substandard and Doubtful categories, the coverage ratio declined sharply since the end of CY-07. The present ratio i.e. 50.6 percent is quite below the industry ratio of 69 percent (see Table 5.2).

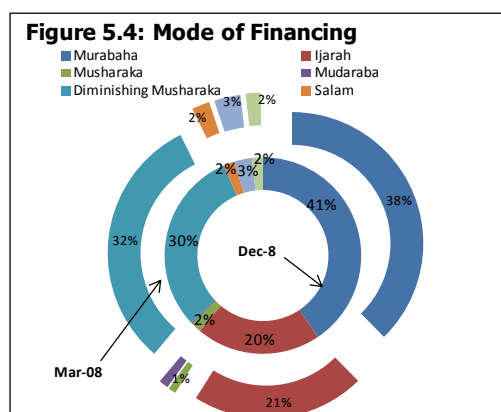
The disaggregated analysis of the deposit mix shows dynamism among different components of deposits. The customer deposit increased by

¹³ For details of GoP Ijara Sukuk please refer to FSCD Circular 13 dated September 06, 2008.



4.3 percent while deposits from financial institutions declined by 15.7 percent over the quarter. Accordingly, the share of customer deposits inched up to 91.4 percent while that of financial institutions deposits receded to 8.6 percent. Of the customer deposits, savings deposits registered a strong increase of 12.6 percent, fixed deposits moderately increased by 3.8 percent while current accounts experienced a decline of 4.3 percent. Resultantly, the composition of deposits slightly shifted towards savings deposits, however fixed deposits continued to be the leading component with 37.9 percent share in total deposits (see Figure 5.3).

Due to sharp decline in financing that came in the backdrop of passive growth in deposits, financing to deposits ratio (FDR) decreased to 66 percent (72 percent in Dec-08 and 83 percent in Sep-08). Moreover, investments in Govt. papers/Sukuks strengthened the fund-based liquidity of Islamic banking.



Composition of financing with slight shift remained stable at the past pattern; Murabaha dominated the financing; though it came off by 12 percent during the quarter, lowering its share in overall financing. Similarly, Ijara, Musharaka and Diminishing Musharaka also declined during the quarter by 1 percent, 47 percent and 2 percent, respectively. Mudaraba, Salam and Istisna portfolios increased over the quarter. Particularly, the increase was most pronounced in Mudaraba portfolio which increased by around 5 times. However, due to its small size, the relative share of Mudaraba, Salam and Istisna remained small as compared to Murabaha and Diminishing Musharaka (see Figure 5.4).

Table 5.3: Income Statement

amount in billion Rupees

	CY04	CY05	CY06	CY07	Mar-08	Dec-08	Mar-09
Markup Income	1.08	3.16	6.38	12.70	4.20	21.95	7.79
Markup Expense	0.48	1.54	3.51	6.80	2.10	11.32	4.11
Net Markup Income	0.60	1.62	2.87	5.90	2.20	10.63	3.69
Provision Expense	0.04	0.18	0.24	0.77	0.16	1.03	0.88
Non Markup Income	0.60	1.21	1.07	2.45	0.50	2.10	0.50
Operating Expense	0.78	1.41	2.86	5.85	2.00	9.66	2.76
Profit Before Tax	0.38	1.24	0.83	1.73	0.50	2.02	0.54
Tax	0.04	0.27	(0.03)	(0.15)	0.10	0.21	0.01
Profit After Tax	0.34	0.98	0.87	1.58	0.40	1.81	0.54

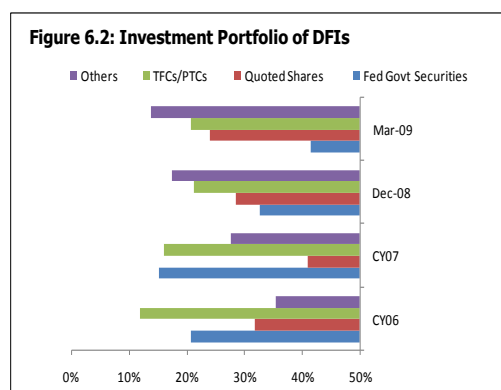
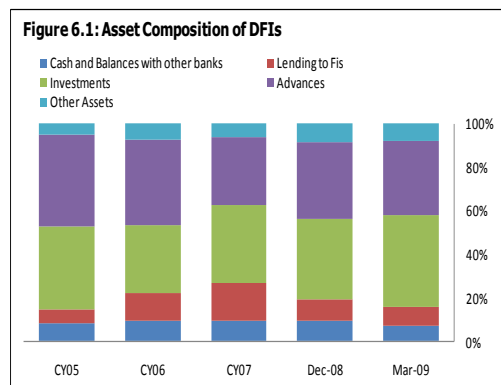
The earnings of Islamic banks remained stable during the quarter under review, as the ROA remained intact at 0.8 percent. The before and after tax profits were more or less proportional to the 2008 results and were higher than corresponding quarter of the last year. The profitability has been augmented by more than proportionate increase in net markup income, which effectively covered the exceptional

increase in provisioning & loan loss charges. The non-markup income remained at the corresponding quarter of last year, while the operating expenses showed a slight increase (see Table 5.3). However, due to stronger increase in net markup income, operating expenses to gross income ratio significantly came off to 66 percent.

6. Development Finance Institutions (DFIs)

Table 6.1: DFIs at a Glance

	CY05	CY06	CY07	Dec-08	Mar-09
Assets	127.6	135.3	112.8	103.7	106.9
Lending to FIs	8.5	17.2	19.3	10.4	9.4
Investments	48.2	42.1	40.5	38.3	45.3
Advances	53.8	53.5	35.4	36.2	36.6
Liabilities	87.8	94.3	69.4	53.8	55.4
Borrowing from FIs	43.7	58.6	51.7	43.1	39.7
Deposits/COLs	38.0	29.4	11.9	5.9	10.5
Equity	39.8	41.0	43.3	49.9	51.4



The first quarter of CY-09 witnessed growth in DFIs' asset- base by 3.1 percent, reaching Rs 106.8 billion. (see Table 6.1). Asset composition of DFIs indicates that their investments and advances account for 76.7 percent of their total assets (72 percent in Dec-08). During the quarter, the earning assets portfolio witnessed significant shift from bank balances and lending to Financial Institutions to investments which increased by 18.3 percentage points (15.9 on YOY basis). As a result, the share of investment portfolio increased by 5.4 percentage points to 42.4 percent. During the quarter, DFIs' advances portfolio registered a marginal increase of 1.1 percent during the quarter (1.9 percent YOY basis) and reached Rs36.6 billion. Lending to financial institutions contracted sharply with its share in total assets receding by 1.3 percentage points to 8.8 percent (13.8 percent Mar-08) (see Figure 6.1).

Breakup of investments indicates that the DFIs' investments in government securities have substantially increased over the last year. Govt. papers account for 41.5 percent of total investments, compared to 16.6 percent in Mar-08. Investments in corporate debt instruments (TFCs/PTCs) have remained around 20.8 percent. The sharp increase in investment in government securities is consistent with the risk averse approach adopted by the financial sector in the wake of loan losses and building credit risk pressures. Investments in quoted shares on the other hand, have dropped to 24 percent compared with 39 percent in Mar-08 because of both volume and value losses in the stock market (see Figure 6.2).

Loan portfolio of DFIs registered a marginal growth of 1.1 percent over the quarter under review (1.9 percent YOY), however, due to decline in balances with banks and lending to Financial institutions, share of loans in their overall assets reached to 34.3 percent from 32 percent in Mar-08.

6.2: Segment wise Loans and NPLs of DFIs

	(In percent)					
	Dec-08			Mar-09		
	Share in Loans	Share in NPLs	NPLs to Loans	Share in Loans	Share in NPLs	NPLs to Loans
Corporate Sector	57.5	44.3	20.2	57.7	47.5	23.2
SMEs Sector	1.1	0.9	22.5	1.0	0.8	23.2
Agriculture Sector	-	-	-	-	-	-
Consumer sector	39.1	54.8	36.8	38.5	51.6	37.8
Credit cards	-	-	-	-	-	-
Auto loans	0.0	0.0	11.3	0.0	0.0	9.1
Consumer durable	0.0	0.0	50.0	0.0	0.0	50.0
Mortgage loans	38.7	54.7	37.1	38.2	51.5	38.1
Other personal loans	0.4	0.1	7.3	0.3	0.1	7.9
Commodity financing	-	-	-	-	-	-
Staff Loans	1.7	-	-	1.6	-	-
Others	0.6	-	-	1.1	-	-
Total	100.0	100.0	26.3	100.0	100.0	28.2

Figure 6.3: Funding Composition of DFIs

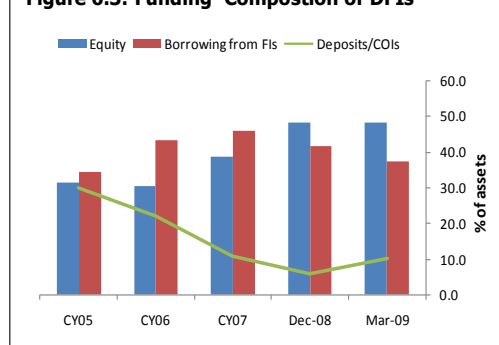


Table 6.3: Key Performance Indicators

	(In percent)				
	CY05	CY06	CY07	Dec-08	Mar-09
Total Capital to Total RWA	32.0	41.0	44.0	49.8	56.1
Tier 1 Capital to Total RWA	29.0	38.0	42.0	50.7	55.6
Capital to total Assets	36.0	31.0	35.0	48.1	48.1
NPLs to total loans	47.0	21.0	9.0	26.0	28.2
Net NPLs to net loans	27.0	13.0	1.0	9.0	12.0
Provision to NPLs	58.0	43.0	88.0	71.0	65.3
Net NPLs to Capital	28.2	17.3	5.0	6.7	8.6
ROA before tax	6.0	2.0	4.0	3.9	1.2
ROA after tax	5.0	2.0	4.0	3.3	0.0
ROE before tax	18.3	7.0	12.4	8.8	2.5
ROE after tax	15.7	7.6	11.3	7.3	0.0
Loans to deposits	142.0	182.0	298.0	616.0	347.4
Net Interest Income to Gross Income	34.3	44.2	39.2	57.7	77.4
Non Interest Income to Gross Income	65.7	55.8	60.8	42.3	22.6
Operating Expense to Gross Income	24.7	37.6	28.9	27.5	31.8

The loan portfolio of DFIs appears to be highly concentrated in corporate and the consumer segments. These two segments account for around 96 percent of total loans portfolio. Due to the high concentration in these two segments the portfolio is left to the vagaries of circumstances and undiversified risk. (See Table 6.2).

Equity and borrowings from financial institutions remained the main sources of funding for DFIs and accounted for 85 percent of the asset base (see Figure 6.3). Inclusion of two new DFIs in CY08 as well as significant capital injections made by other institutions has made equity the largest source of funding at 48 percent of asset base (42.7 in Mar-08). Borrowings as a percentage of total assets registered a 4.5 percentage points decline to 37.1 percent; during the quarter, on the other hand deposits/COIs which have been declining since CY05 increased to Rs.10 billion enhancing their share in overall assets from 5.7 percent to 10 percent during the quarter.

A comfortably strong capital base provides sufficient cushion to withstand unexpected losses from business operations. As a result of progressive capital injection over the last few years, entry of new institutions, increase in investments in risk-free Government papers, capital adequacy indicators of DFIs have improved. CAR improved to 56.1 percent in Mar-09 from 49.8 percent in Dec-08 (45.3 percent in Mar-08). Similarly Tier-I capital to RWAs ratio too increased by 4.9 percentage points to 55.6 percent over the same period (44.8 percent in Mar-08) (see Table 6.2). The noticeable increase in the equity of the DFIs is also evident from the improved capital to asset ratio, which improved to 48.1 percent from the level of 42.7 percent in Mar-08. The ratio has improved since CY05 when it was 36 percent.

Asset quality indicators however, continue to deteriorate due to worsening business environment. Non-performing loans of DFIs registered an increase of 8.1 percent to Rs.12.7 billion (Rs.8.3 billion Mar-08). As a result NPLs to Loan ratio increased by 2.2 percent to 28.2

percent over the quarter. However, due to partial provisioning coverage of fresh NPLs, the Net NPLs increased at swift pace, net NPLs to Loan ratio increased by 3 percentage points to 12 percent. The deterioration of asset quality indicators does not augur well for the profitability of the DFIs.

With increased provision charges and dry spells in the capital market, the quarter under review remained uneventful for the DFIs with regard to profitability. Profit before tax stood at Rs. 316 million against Rs. 7,418 million in the corresponding period of Mar-08. (Rs.4,272 million in CY08). The ROA before tax declined from 3.9 percent in Dec-08 to 1.2 percent in Mar-09. Similarly, the ROE before tax declined from 8.8 percent in Dec-08 to 2.5 percent in Mar-09. The tax impact further dampened the earnings which translated into the loss after tax of loss stood at Rs 0.1 million.

Non mark-up income has previously been a major source of income for DFIs. The non-mark up income to gross income ratio declined from 42 percent in Dec-08 to 22.6 percent in Mar-09. On the flip side, the ratio of net interest income to gross income rose from 57.7 percent in Dec-08 to 77.4 percent in Mar-09. Due to slowdown in overall earnings, operating expenses as percentage of gross income also increased to 31.8 percent (27.5 percent in Dec-08).

The advances and the funding structure of DFIs both warrant broad basing, while the advances are largely concentrated in a few segments, heavy reliance on high cost borrowings from financial institutions puts strains on the profitability of the institutions. DFIs ought to diversify their funding sources, particularly by increasing deposit base as well as exert concerted efforts to expand their lending operations into the underserved but promising sectors of the economy, in order to achieve their objective of financing medium and long-term projects in industry and agriculture.

Special Section 2: Analysis of Financial Derivative Business

Financial derivative business started in Pakistan in 2003. Initially banks were allowed to undertake the business of financial derivatives after getting specific transactional approval from SBP. In 2004, with an objective to develop an over the counter (OTC) financial derivatives market in the country, SBP allowed Banks/DFIs to undertake derivatives business, provided they meet the eligibility criteria and obtain Authorized Derivatives Dealer (ADD) or Non Market Maker Financial Institution (NMI) status from SBP. For the purpose, SBP issued Financial Derivatives Business Regulations (FDBR), which not only contains the regulatory framework for the OTC financial derivative transactions but also includes specifics related to permissible derivative transactions. The permitted types of transactions include G-7 Foreign Currency Options, PKR Forward Rate Agreements (FRA) and PKR Interest Rate Swaps (IRS). However, banks/DFIs can undertake any other type of transaction with SBP's prior approval.

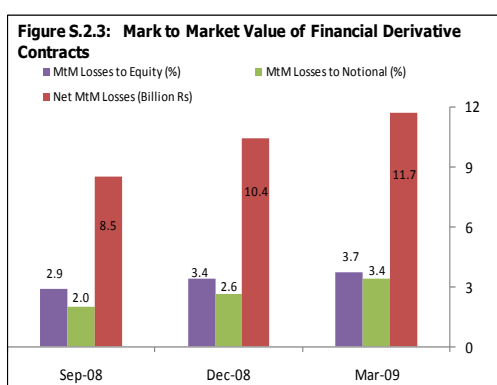
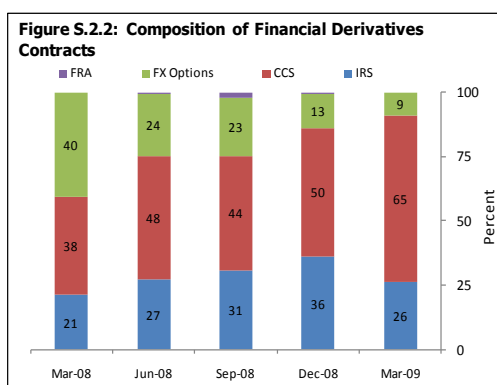
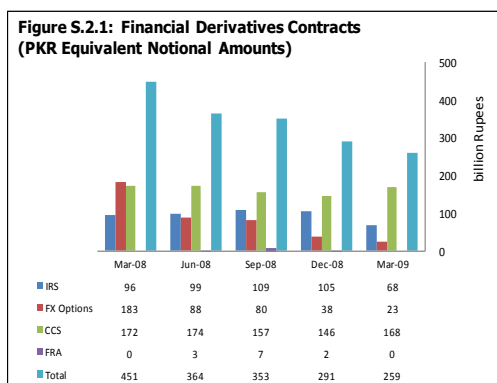
So far, SBP has granted ADD status to five financial institutions, however no institution has obtained the status of NMI. Any institution other than the five ADDs interested in undertaking derivative business requires prior approval from SBP.

Analysis of Derivative Business

The following paragraphs discuss the trend, composition, and mark-to-market dynamics of financial derivatives since corresponding quarter of the last year.

The financial derivative business witnessed significant decline over the last one year or so and this trend prevailed during the quarter under review as well. Outstanding notional amount of all derivatives declined by 11 percent over the quarter to Rs259 billion¹⁴ giving 43 percent decrease on YoY basis. However, the number of outstanding contracts increased

¹⁴ The amount pertains to 8 banks including 5 ADDs, excluding the hedging transactions with Resident/non Resident banks.



during the quarter to 423 (392 in Dec-08 and 458 in Sep-08). Individual components of the derivative portfolio showed divergent trends (see Figure S.2.1), with the relative component share changes over the year (see Figure S.2.2).

Most significant decline was observed in **Foreign Exchange Options (FX Options)**¹⁵ which declined by around 87 percent over the year to Rs23 billion and their relative share declined to around 9 percent by the end of Mar-09. These contracts constitute the third major component of banks' derivative portfolio against the leading share a year ago.

Cross Currency Swaps (CCS) which constitutes the largest share of the value of total outstanding derivatives contracts increased by 15 percent during the quarter, while on YoY basis declined by 2 percent. Due to decline in all other components, the share of CCS significantly increased to 65 percent (50 percent in Dec-08 and 38 percent in Mar-08). During the last two quarter, CCS has followed a declining trend which reversed during the quarter under review. The leading factor behind the popularity of CCS has been the high gap between local and international interest rates that induced the local corporate with large export volumes to swap their local currency exposures with LIBOR or EURIBOR.

Interest Rate Swaps (IRS)¹⁶ registered a decline of 35 percent during the quarter under review, YoY basis declining by 29 percent. This sharp decline during the quarter mainly signifies the expectations of decline in PKR interest rates among market participants. These expectations later on were also corroborated by cut in SBP Policy Rate during April 2009.

All **Forward Rate Agreements (FRAs)**¹⁷ which were a recent phenomenon in Pakistani derivative market got matured or cancelled during the quarter under review. Nevertheless,

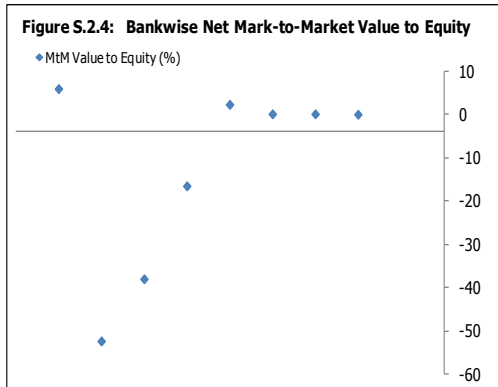
¹⁵ As stated in the FDBR, dealing in FX options is permitted in G-7 currencies only. While there is no restriction on the minimum or maximum size of 'notional principal' amounts of FX options, the maximum tenor is restricted to one year.

¹⁶ As per FDBR, IRS transactions are permitted in PKR only, with a maximum tenor of 5 years and there is no restriction on the minimum or maximum size of 'notional principal' amounts of IRS.

¹⁷ In the FDBR, dealing in FRAs is permitted in PKR only, with a maximum tenor of 2 years.

their share had remained negligible in the value of total outstanding derivatives transactions.

The outstanding financial derivatives transactions pertain to eight banks, including 5 ADDs. These banks belong to different banking group: 5 LPBs, 2 FBs and a PSCB. The mark-to-market position shows that four banks are carrying mark-to-market losses on their derivative books while on banking group basis all groups are carrying negative values. Total mark-to-market losses during the quarter under review increased by 12 percent to Rs11.7 billion (Rs10.4 billion in Dec-08). These mark-to-market losses come to around 3.7 percent of the equity of banks engaged in derivate business and 3.4 percent of outstanding notional principal amounts (see Figure S.2.3). However, a couple of banks have significantly risky exposures that could create further stress in case of any adverse movements in underlying prices (see Figure S.2.4).



Group wise Balance Sheets and Income Statements of Banks **as of March 31, 2009**

(Amount in million rupees)

FINANCIAL POSITION	PSCB	LPB	FB	SB	CB	All Banks
ASSETS						
Cash & Balances With Treasury Banks	133,056	318,537	32,956	1,999	484,549	486,548
Balances With Other Banks	38,295	113,887	16,454	15,589	168,635	184,224
Lending To Financial Institutions	24,837	161,084	29,340	763	215,262	216,025
Investments - Net	225,005	1,019,585	41,212	12,608	1,285,802	1,298,410
Advances - Net	545,955	2,298,592	97,157	82,250	2,941,704	3,023,954
Operating Fixed Assets	28,095	190,820	3,921	5,014	222,836	227,850
Deferred Tax Assets	14,734	33,678	4,496	0	52,908	52,909
Other Assets	64,111	165,517	13,928	10,441	243,555	253,996
TOTAL ASSETS	1,074,087	4,301,700	239,464	128,664	5,615,251	5,743,916
LIABILITIES						
Bills Payable	7,395	54,372	4,276	883	66,042	66,925
Borrowings From Financial Institution	57,810	376,627	24,686	87,317	459,123	546,440
Deposits And Other Accounts	837,359	3,220,269	149,170	11,402	4,206,799	4,218,201
Sub-ordinated Loans	-	35,596	-	3,405	35,596	39,002
Liabilities Against Assets Subject To Finance Lease	62	370	-	18	432	450
Deferred Tax Liabilities	3,157	6,154	248	106	9,560	9,666
Other Liabilities	49,530	163,698	26,690	28,956	239,918	268,874
TOTAL LIABILITIES	955,313	3,857,087	205,070	132,088	5,017,470	5,149,558
NET ASSETS	118,774	444,613	34,394	(3,424)	597,781	594,357
NET ASSETS REPRESENTED BY:						
Share Capital	19,545	230,971	32,515	15,506	283,032	298,538
Reserves	28,422	131,157	76	2,447	159,655	162,102
Unappropriated Profit	47,673	53,152	2,020	(24,735)	102,845	78,109
Share Holders' Equity	95,640	415,280	34,611	(6,782)	545,531	538,749
Surplus/Deficit On Revaluation Of Assets	23,134	29,333	(216)	3,358	52,250	55,608
TOTAL	118,774	444,613	34,394	(3,424)	597,781	594,357
OPERATING POSITION						
Mark-Up/ Return/Interest Earned	23,075	114,740	5,616	3,500	143,431	146,931
Mark-Up/ Return/Interest Expenses	14,443	60,981	3,100	1,526	78,524	80,049
Net Mark-Up / Interest Income	8,632	53,758	2,516	1,974	64,907	66,882
Provisions & Bad Debts Written Off Directly/(Reversals)	2,009	14,772	1,339	(136)	18,120	17,985
Net Mark-Up / Interest Income After Provision	6,623	38,986	1,177	2,110	46,787	48,897
Fees, Commission & Brokerage Income	1,929	7,496	463	40	9,888	9,928
Dividend Income	309	723	1	66	1,032	1,099
Income From Dealing In Foreign Currencies	1,198	3,301	1,087	8	5,586	5,594
Other Income	520	2,815	523	906	3,859	4,765
Total Non - Markup / Interest Income	3,955	14,335	2,075	1,021	20,365	21,386
	10,578	53,322	3,252	3,131	67,152	70,283
Administrative Expenses	6,036	33,280	2,672	1,807	41,989	43,796
Other Expenses	16	218	18	0	253	253
Total Non-Markup/Interest Expenses	6,053	33,499	2,690	1,808	42,241	44,049
Profit before Tax and Extra ordinary Items	4,526	19,823	562	1,323	24,911	26,234
Extra ordinary/unusual Items - Gain/(Loss)	-	-	-	-	-	-
PROFIT/ (LOSS) BEFORE TAXATION	4,526	19,823	562	1,323	24,911	26,234
Taxation	2,121	7,517	328	456	9,966	10,423
PROFIT/ (LOSS) AFTER TAX	2,405	12,306	234	866	14,945	15,811

Financial Soundness Indicators

Indicators	2005	2006	2007	Mar-08	Dec-08	Mar-09
CAPITAL ADEQUACY						
Risk Weighted CAR						
Public Sector Commercial Banks	14.5	15.2	17.8	15.5	12.8	14.0
Local Private Banks	10.6	12.7	12.8	12.0	12.2	12.7
Foreign Banks	16.4	15.0	13.5	14.9	19.8	22.4
Commercial Banks	11.9	13.3	13.8	12.8	12.6	13.3
Specialized Banks	(7.7)	(8.3)	(7.8)	24.8	(2.3)	(2.5)
All Banks	11.3	12.7	13.2	13.0	12.2	12.9
Tier 1 Capital to RWA						
Public Sector Commercial Banks	8.8	11.1	13.0	11.3	10.1	11.4
Local Private Banks	8.3	10.4	10.5	9.9	10.3	10.7
Foreign Banks	16.1	14.3	12.9	14.2	19.3	21.9
Commercial Banks	9.1	10.8	11.1	10.3	10.7	11.3
Specialized Banks	(13.6)	(13.3)	(13.5)	19.8	(7.6)	(7.5)
All Banks	8.3	10.0	10.5	10.5	10.2	10.8
Capital to Total Assets						
Public Sector Commercial Banks	12.6	12.2	13.7	13.7	11.9	11.1
Local Private Banks	7.0	9.2	10.2	10.1	10.1	10.3
Foreign Banks	9.5	10.1	11.2	10.3	13.9	14.4
Commercial Banks	8.4	9.9	10.9	10.8	10.7	10.6
Specialized Banks	(8.1)	(8.0)	(5.5)	(6.2)	(2.5)	(2.7)
All Banks	7.9	9.4	10.5	10.4	10.4	10.3
ASSET QUALITY						
NPLs to Total Loans						
Public Sector Commercial Banks	10.0	9.0	8.4	9.4	12.3	17.5
Local Private Banks	6.4	5.2	6.0	6.5	7.8	9.7
Foreign Banks	1.2	1.0	1.6	1.7	2.9	3.6
Commercial Banks	6.7	5.7	6.3	6.9	8.5	11.0
Specialized Banks	46.0	39.1	34.3	34.2	28.9	29.0
All Banks	8.3	6.9	7.2	7.7	9.1	11.5
Provision to NPLs						
Public Sector Commercial Banks	86.8	84.5	89.0	87.5	78.8	65.3
Local Private Banks	76.4	78.7	87.2	86.0	73.2	71.2
Foreign Banks	145.9	191.7	157.0	138.4	94.2	81.3
Commercial Banks	80.4	81.5	88.2	86.8	74.9	69.5
Specialized Banks	64.8	64.1	68.6	67.1	72.1	66.4
All Banks	76.7	77.8	85.1	84.1	74.7	69.2
Net NPLs to Net Loans						
Public Sector Commercial Banks	1.5	1.5	1.0	1.3	2.9	6.9
Local Private Banks	1.6	1.1	0.8	1.0	2.2	3.0
Foreign Banks	(0.6)	(1.0)	(0.9)	(0.7)	0.2	0.7
Commercial Banks	1.4	1.1	0.8	1.0	2.3	3.6
Specialized Banks	23.1	18.7	14.0	14.6	10.2	12.1
All Banks	2.1	1.6	1.1	1.3	2.5	3.9
Net NPLs to Capital						
Public Sector Commercial Banks	5.5	6.4	3.4	4.8	12.9	31.6
Local Private Banks	13.0	7.1	4.2	5.2	12.7	15.4
Foreign Banks	(3.0)	(5.1)	(4.1)	(3.1)	0.5	2.0
Commercial Banks	9.0	6.2	3.7	4.8	12.1	17.9
Specialized Banks	-	-	-	-	-	-
All Banks	14.3	9.7	5.6	6.8	13.6	19.6
EARNINGS						
Return on Assets (Before Tax)						
Public Sector Commercial Banks	3.3	4.0	3.6	1.3	1.4	1.7
Local Private Banks	2.7	3.1	2.0	2.5	1.8	1.9
Foreign Banks	3.6	3.2	1.5	1.7	0.2	1.0
Commercial Banks	2.9	3.2	2.3	2.3	1.7	1.8
Specialized Banks	(1.0)	(1.3)	1.4	0.0	3.1	3.8
All Banks	2.8	3.1	2.2	2.2	1.7	1.8
Return on Assets (After Tax)						
Public Sector Commercial Banks	2.2	2.7	2.5	0.6	1.1	0.9
Local Private Banks	1.8	2.1	1.4	1.7	1.2	1.2
Foreign Banks	2.5	2.1	0.7	0.8	(0.5)	0.4
Commercial Banks	1.99	2.19	1.56	1.5	1.1	1.1
Specialized Banks	(1.2)	(1.8)	0.7	0.0	2.7	2.4
All Banks	1.89	2.08	1.54	1.4	1.2	1.1

Financial Soundness Indicators

Indicators	2005	2006	2007	Mar-08	Dec-08	Mar-09
ROE (Avg. Equity & Surplus) (Before Tax)						
Public Sector Commercial Banks	30.7	32.4	27.2	9.6	11.2	14.7
Local Private Banks	40.1	36.2	20.4	24.7	18.3	18.1
Foreign Banks	38.9	30.0	13.5	16.0	1.6	6.7
Commercial Banks	37.2	34.7	21.9	20.7	15.9	16.8
Specialized Banks	-	-	-	-	-	-
All Banks	38.2	35.2	22.6	20.7	16.7	17.7
ROE (Avg. Equity & Surplus) (After Tax)						
Public Sector Commercial Banks	20.9	21.7	19.5	4.7	8.7	7.8
Local Private Banks	27.2	25.0	13.9	16.6	12.1	11.3
Foreign Banks	27.1	20.4	6.3	7.1	(4.1)	2.8
Commercial Banks	25.4	23.7	15.0	13.3	10.7	10.1
Specialized Banks	-	-	-	-	-	-
All Banks	25.8	23.8	15.5	13.2	11.3	10.7
NII/Gross Income						
Public Sector Commercial Banks	71.3	69.5	65.9	66.2	65.8	68.6
Local Private Banks	73.0	73.5	70.8	71.5	73.4	78.9
Foreign Banks	61.5	65.8	59.1	57.9	59.5	54.8
Commercial Banks	71.3	72.1	69.3	69.8	71.4	76.1
Specialized Banks	87.7	40.1	42.8	56.2	50.3	65.9
All Banks	72.0	70.9	68.3	69.1	70.7	75.8
Cost / Income Ratio						
Public Sector Commercial Banks	34.3	31.8	30.2	35.0	38.2	48.1
Local Private Banks	43.1	40.7	45.2	46.2	50.6	49.2
Foreign Banks	42.2	49.8	56.4	52.8	68.1	58.6
Commercial Banks	41.2	39.4	42.6	44.3	49.1	49.5
Specialized Banks	47.8	62.6	52.5	45.1	49.2	60.4
All Banks	41.5	40.3	43.0	44.6	49.1	49.9
LIQUIDITY						
Liquid Assets/Total Assets						
Public Sector Commercial Banks	35.6	33.9	37.5	32.3	27.6	31.4
Local Private Banks	32.4	31.1	32.5	30.6	26.6	29.5
Foreign Banks	41.8	41.0	41.5	39.0	45.3	49.6
Commercial Banks	33.9	32.2	33.8	31.2	27.6	30.7
Specialized Banks	25.8	23.0	25.9	22.1	24.3	21.6
All Banks	33.7	31.9	33.6	31.0	27.5	30.5
Liquid Assets/Total Deposits						
Public Sector Commercial Banks	44.7	42.6	47.7	41.6	35.8	40.3
Local Private Banks	40.3	40.6	42.8	40.4	34.8	39.3
Foreign Banks	57.9	61.1	61.0	54.8	71.3	79.6
Commercial Banks	42.7	42.0	44.4	41.2	36.3	41.0
Specialized Banks	183.2	205.4	229.6	204.3	233.8	243.7
All Banks	43.5	42.7	45.1	41.7	36.9	41.5
Advances/Deposits						
Public Sector Commercial Banks	59.8	64.6	60.0	65.9	69.6	65.2
Local Private Banks	70.8	74.5	70.1	72.2	75.7	71.4
Foreign Banks	68.7	80.1	75.2	66.6	69.1	65.1
Commercial Banks	68.4	72.7	68.1	70.7	74.3	69.9
Specialized Banks	400.7	528.4	507.2	544.5	602.7	721.3
All Banks	70.2	74.6	69.8	72.3	75.9	71.7

Selected Indicators for Different Categories of Banks
in terms of Size March 31, 2009

(In percent)

Indicators	Top 5 Banks	Top 10 Banks	Top 20 Banks	Industry
Share of Total Assets	51.9	72.9	92.7	100.0
Share of Total Deposits	54.6	76.9	93.6	100.0
Share of Gross Income	58.9	75.2	94.0	100.0
Share of Risk Weighted Assets	52.4	72.5	92.5	100.0
Capital Adequacy				
Capital/RWA	13.8	12.6	12.7	12.9
Tier 1 Capital / RWA	11.3	10.3	10.5	10.8
Net Worth / Total Assets	10.5	9.7	10.1	10.3
Asset Composition				
Sectoral Distribution of Loans				
- Corporate Sector	52.2	75.1	93.1	100.0
- SMEs	42.3	63.2	89.5	100.0
- Agriculture	28.9	40.6	94.6	100.0
- Consumer Finance	50.7	75.5	94.5	100.0
- Commodity Financing	80.2	92.3	99.4	100.0
- Staff Loans	58.7	74.4	91.3	100.0
- Others	84.3	94.9	95.2	100.0
- Total	52.7	73.9	93.4	100.0
NPLs / Gross Loans	10.2	10.8	11.2	11.5
Net NPLs / Capital	14.9	18.8	19.4	19.6
Earning & Profitability				
ROA	2.1	1.5	1.4	1.1
ROE	20.5	14.5	13.5	10.7
Net Interest Income / Gross Income	79.6	78.2	75.8	75.8
Income from Trading & Foreign Exchange / Gross Income	15.7	17.3	17.4	17.6
Non-Interest Expense / Gross Income	37.9	44.3	46.4	49.9
Liquidity				
Liquid Assets / Total Assets	30.4	29.7	30.1	30.5
Liquid Assets held in Govt. Securities / Total Liquid Assets	50.4	52.4	53.4	51.9
Liquid Assets / Total Deposits	39.4	38.4	40.6	41.5

Bank-wise Major Statistics March 31, 2009

(Amount in million Rupees)

S. No.	Name of the Banks	Assets	Deposits	Equity
Public Sector Commercial Banks				
1	National Bank of Pakistan	844,726	640,509	110,172
2	First Women Bank Limited	7,243	5,849	1,162
3	The Bank of Punjab	192,182	169,236	2,564
4	The Bank of Khyber	29,935	21,765	4,875
Local Private Banks				
5	Allied Bank Limited	347,697	284,683	24,810
6	Bank Alfalah Limited	328,824	273,259	21,258
7	Askari Bank Limited	204,572	157,324	13,621
8	Bank Al Habib Limited	198,101	156,184	11,968
9	Mybank Limited	39,158	26,060	6,135
10	SAMBA Bank Limited	21,414	9,155	5,310
11	Atlas Bank Limited	30,404	24,796	3,411
12	Faysal Bank Limited	149,749	106,061	11,244
13	Habib Bank Limited	712,637	569,231	65,810
14	KASB Bank Limited	59,801	42,550	9,137
15	Arif Habib Bank Limited	29,196	20,718	5,851
16	JS Bank Limited	23,854	13,587	5,489
17	MCB Bank Limited	456,430	338,311	62,256
18	United Bank Limited	622,378	469,273	49,698
19	The Royal Bank of Scotland Limited	103,855	74,961	9,888
20	Habib Metropolitan Bank Limited	189,280	119,357	16,898
21	BankIslami Pakistan Limited	22,935	16,514	5,110
22	Emirates Global Islamic Bank	17,727	12,284	3,998
23	Soneri Bank Limited	88,651	66,324	7,670
24	Saudi Pak Commercial Bank Limited	61,882	44,804	4,043
25	NIB Bank Limited	185,597	107,899	40,612
26	Meezan Bank Limited	89,178	72,975	6,501
27	Dubai Islamic Bank Pakistan Limited	29,369	22,760	5,118
28	Standard Chartered Bank	278,515	186,234	43,686
29	Dawood Islamic Bank Limited	10,496	4,965	5,091
Foreign Banks				
30	Albaraka Islamic Bank B.S.C. (E.C.), Pakistan Operations	24,292	18,224	2,250
31	Citibank N.A. (Pakistan Operations)	109,291	65,213	9,621
32	Deutsche Bank AG (Pakistan Operations)	15,667	4,344	4,223
33	HSBC Bank Middle East Limited - (Pakistan Operations)	47,606	38,793	5,154
34	Oman International Bank S.A.O.G (Pakistan Operations)	3,443	488	2,756
35	The Bank of Tokyo-Mitsubishi UFJ Limited (Pakistan Operations)	8,420	3,119	3,795
36	Barclays Bank PLC (Pakistan Operations)	30,745	18,989	6,595
Specialized Banks				
37	The Punjab Provincial Cooperative Bank Ltd	14,705	1,657	4,907
38	Industrial Development Bank of Pakistan	4,827	3,857	(28,544)
39	Zarai Taraqiati Bank Limited	103,195	3,811	18,189
40	SME Bank Limited	5,937	2,077	2,025
Total		5,743,916	4,218,201	594,357

Results of Stress Test of Banking System

Position Based on March 31, 2009

		Number of Banks with CAR		
		< 0%	0% - 9%	>9%
Pre-Shock		1	3	36
Post-Shock				
Credit Shocks				
C-1	15% of performing loans moving to substandard, 15% of substandard to doubtful, 25% doubtful to loss	1	9	30
C-2	Tightening of loan classification i.e. all NPLs under OAEM require 25% provisioning, all NPLs under substandard require 50% and all NPLs in doubtful category require 100% provisioning.	2	6	32
C-3	Deterioration of loans to the textile sector (25%) directly downgraded to doubtful category	2	10	28
C-4	25% of consumer loans (auto loans, personal loans & consumer durables only) classified into doubtful category.	1	6	33
C-5	Default of three largest exposures (Fund Based exposures)	3	18	19
Market Shocks				
Interest Rate Shocks				
IR-1	An increase in interest rates by 500 basis points.	1	8	31
IR-2	Shift coupled with flattening of the yield curve by increasing 500,300 and 200 basis points in the three maturities respectively.	1	4	35
Exchange Rate Shocks				
ER-1	Depreciation of exchange rate by 25%	1	4	35
ER-2	Appreciation of exchange rate by 25%	2	2	36
ER-3	Depreciation of PRs against all currencies (25%) and deterioration of unhedged FX loans	1	5	34
Equity Price Shocks				
Eq-1	Fall in the equity prices by 50%.	1	6	33
Eq-2	Fall in the equity prices by 60%.	1	6	33
Eq-3	Fall in the equity prices by 70%.	1	6	33
Combined Credit & Market Shocks				
COMB-1	Interest rates increase (5%), deterioration of loans to the textile sector (25%) directly downgraded to doubtful category, and fall in equity prices by 50%.	2	16	22
COMB-2	Interest rates increase (5%), migration of loan portfolio (performing to substandard: 15%, substandard to doubtful: 15%, doubtful to loss: 20%), stock market price depreciation (50%).	2	15	23
Liquidity Shock		Number of Banks Becoming Illiquid after Shock		
		3 days	4 days	5 days
L-1	Withdrawal of customer deposits by 2%, 5%, 10%, 10% and 10% for five consecutive days respectively.	1	3	6

Group wise Balance Sheets and Income Statements of Islamic Banks/Branches - March 31, 2009

(Amount in million Rupees)

Financial Position	Islamic Banks	Islamic Banking Branches	Total Islamic Banking
ASSETS			
Cash & Balances With Treasury Banks	14,611	6,740	21,351
Balances With Other Banks	17,398	7,423	24,820
Due from Financial Institutions	21,779	100	21,879
Investments - Net	33,313	15,657	48,970
Financing - Net	89,308	46,877	136,184
Operating Fixed Assets	8,267	2,967	11,234
Deferred Tax Assets	1,062	0	1,062
Other Assets	8,260	4,627	12,887
TOTAL ASSETS	193,997	84,391	278,388
LIABILITIES	0	0	0
Bills Payable	2,214	545	2,759
Due to Financial Institution	7,084	6,504	13,588
Deposits And Other Accounts	147,722	58,518	206,240
Sub-ordinated Loans	0	0	0
Liabilities Against Assets Subject To Finance Lease	70	0	70
Deferred Tax Liabilities	304	1	306
Other Liabilities	8,535	10,472	19,007
TOTAL LIABILITIES	165,930	76,040	241,970
NET ASSETS	28,067	8,351	36,418
NET ASSETS REPRESENTED BY: -	0	0	0
Share Capital	28,183	6,228	34,411
Reserves	919	5	924
Unappropriated Profit	(923)	1,431	509
Share Holders' Equity	28,180	7,664	35,844
Surplus/Deficit On Revaluation Of Assets	(113)	687	574
TOTAL	28,067	8,351	36,418
PROFIT AND LOSS STATEMENT			
Mark-Up Income	5,309	2,483	7,792
Mark-Up Expenses	2,735	1,371	4,106
Net Mark-Up	2,574	1,111	3,685
Provisions & Bad Debts Written Off Directly/(Reversals)	697	181	879
Net Mark-Up After Provision	1,877	930	2,807
Fees, Commission & Brokerage Income	219	74	293
Dividend Income	33	9	42
Income From Dealing In Foreign Currencies	90	12	102
Other Income	20	44	64
Total Non - Markup	362	139	501
	2,239	1,069	3,308
Administrative Expenses	2,187	544	2,732
Other Expenses	17	15	32
Total Non-Markup	2,204	559	2,764
Profit before Tax and Extra ordinary Items	35	510	544
Extra ordinary/unusual Items -- Gain/(Loss)	0	0	0
PROFIT/ (LOSS) BEFORE TAXATION	35	510	544
Taxation	9	0	9
PROFIT/ (LOSS) AFTER TAX	26	510	536

Balance Sheets and Income Statements of DFIs-March 31, 2009

(Amount in million rupees)

Financial Position	All DFIs
ASSETS	
Cash & Balances With Treasury Banks	197.9
Balances With Other Banks	7,015.2
Lending To Financial Institutions	9,378.4
Investments - Net	45,284.8
Advances - Net	36,634.7
Operating Fixed Assets	3,061.1
Deferred Tax Assets	763.2
Other Assets	4,537.7
TOTAL ASSETS	106,873.0
LIABILITIES	
Bills Payable	-
Borrowings From Financial Institution	39,652.9
Deposits And Other Accounts	10,544.9
Sub-ordinated Loans	-
Liabilities Against Assets Subject To Finance Lease	38.2
Deferred Tax Liabilities	-
Other Liabilities	5,202.4
TOTAL LIABILITIES	55,438.4
NET ASSETS	51,434.6
NET ASSETS REPRESENTED BY: -	
Share Capital	44,013.9
Reserves	7,590.4
Unappropriated Profit	(975.1)
Share Holders' Equity	50,629.2
Surplus/Deficit On Revaluation Of Assets	805.4
TOTAL	51,434.6
OPERATING POSITION	39903
Mark-Up/ Return/Interest Earned	2,996.9
Mark-Up/ Return/Interest Expenses	1,525.9
Net Mark-Up / Interest Income	1,471.0
Provisions & Bad Debts Written Off Directly/(Reversals)	907.1
Net Mark-Up / Interest Income After Provision	563.8
Fees, Commission & Brokerage Income	50.4
Dividend Income	64.3
Income From Dealing In Foreign Currencies	19.7
Other Income	295.8
Total Non - Markup / Interest Income	430.3
	994.2
Administrative Expenses	595.2
Other Expenses	10.2
Total Non-Markup/Interest Expenses	605.4
Profit before Tax and Extra ordinary Items	388.7
Extra ordinary/unusual Items -- Gain/(Loss)	72.1
PROFIT/ (LOSS) BEFORE TAXATION	316.6
Taxation	316.7
PROFIT/ (LOSS) AFTER TAX	(0.1)

Capital Structure and Capital Adequacy Ratio of All Banks and DFIs as of March 31, 2009

(Amount in million Rupees)								
Equity		All Banks and DFIs	All Banks	PSPB	LPB	FB	SB	DFIs
1.1	Fully Paid-up Capital/Capital Deposited with SBP	346,169.7	302,155.8	19,545.4	234,589.5	32,514.8	15,506.2	44,013.9
1.2	Balance in Share Premium Account	31,006.6	31,006.6	37.9	30,968.7	-	-	-
1.3	Reserve for issue of Bonus shares	7,329.1	7,329.1	-	7,329.1	-	-	-
1.4	General Reserves as disclosed on the Balance Sheet (including statutory reserve)	106,705.7	98,342.1	22,429.9	73,695.2	(230.2)	2,447.1	8,363.6
1.5	Un-appropriated/Unremitted profits (net of accumulated losses, if any)	76,163.3	78,030.7	48,616.0	51,959.8	2,344.3	(24,889.4)	(1,867.4)
1.6	Minority interest	3,812.3	3,812.3	-	3,812.3	-	-	-
1.7	Sub-Total (1.1 to 1.5)	571,186.7	520,676.6	90,629.2	402,354.7	34,628.9	(6,936.1)	50,510.1
	Deductions							
1.8	Goodwill	59,346.1	59,330.3	430.8	58,647.8	198.1	53.6	15.8
1.9	Shortfall in Provisions required against Classified assets	396.0	396.0	-	220.2	-	175.8	-
1.10	Deficit on account of revaluation of AFS investment	9,387.0	7,497.2	3,440.7	2,958.0	401.0	697.5	1,889.8
1.11	Any increase in equity capital resulting from a securitization transaction	232.2	232.2	-	232.2	-	-	-
1.12	Investments in TFCs of other banks	-	-	-	-	-	-	-
1.13	Other Deductions	9,398.2	8,363.6	1,692.0	6,513.9	-	157.7	1,034.6
1.14	Sub-Total (1.7 to 1.10)	78,759.5	75,819.3	5,563.5	68,572.2	599.0	1,084.7	2,940.2
1.15	Total Eligible Tier 1 capital	492,427.2	444,857.3	85,065.7	333,782.5	34,029.9	(8,020.8)	47,569.9
	Supplementary Capital							
2.1	Freely available General Provisions or reserves for loan losses-up to maximum of 1.25% of Risk Weighted Assets	16,569.6	16,343.4	4,221.9	10,157.0	804.8	1,159.7	226.2
2.2	Revaluation reserves eligible upto 45%	29,997.0	28,787.0	11,463.9	15,338.8	-	1,984.3	1,209.9
2.3	Foreign Exchange Translation Reserves	18,884.3	18,884.3	5,954.2	12,930.1	-	-	-
2.4	Undisclosed reserves	-	-	-	-	-	-	-
2.5	Subordinated debt-up to maximum of 50% of total equity	32,629.1	32,629.1	-	29,424.7	-	3,204.3	-
2.6	Total Tier 2 Supplementary Capital(2.1 - 2.5)	98,079.9	96,643.8	21,640.0	67,850.6	804.8	6,348.3	1,436.1
	Deductions							
	Other deductions	9,398.2	8,363.6	1,692.0	6,513.9	-	157.7	1,034.6
	Total Deductions	9,398.2	8,363.6	1,692.0	6,513.9	-	157.7	1,034.6
	Total eligible tier 2 capital	88,681.7	88,280.2	19,948.1	61,336.7	804.8	6,190.6	401.5
2.7	Eligible tier 3 (as worked out in 3.9 below)							
2.8	Total Supplementary Capital eligible for MCR(maximum upto 100% of Total Equity)	87,278.1	88,280.2	19,327.9	61,336.7	804.8	5,407.2	401.5
2.9	TOTAL CAPITAL (1.12+2.8)	579,705.3	533,137.5	104,393.6	395,119.3	34,834.7	(2,613.6)	47,971.4
	Risk Weighted Amounts							
3.3	Total Credit Risk Weighted Assets	3,496,643.6	3,443,566.4	605,591.5	2,625,797.5	122,824.7	89,352.7	53,077.2
3.4	Total Market Risk Weighted Assets	160,372.6	138,431.6	37,271.8	93,202.0	7,914.0	43.9	21,941.0
	Total Operational Risk Assets	544,542.9	534,076.0	101,263.5	391,002.6	24,570.4	17,239.5	10,466.9
3.5	Total Risk Weighted Amount	4,201,559.1	4,116,074.0	744,126.7	3,110,364.6	155,309.2	106,636.1	85,485.0
	Capital Adequacy Ratios (CAR)							
	Credit Risk Capital Adequacy Ratio	0.2	0.2	0.2	0.2	0.3	(0.0)	0.9
	Tier 1 capital to Total Risk Weighted Amount	0.1	0.1	0.1	0.1	0.2	(0.1)	0.6
	Total Capital Adequacy Ratio	0.1	0.1	0.1	0.1	0.2	(0.0)	0.6
	Tier 2 capital to Total Risk Weighted Amount	0.0	0.0	0.0	0.0	0.0	0.1	0.0
	OTHER DEDUCTIONS FROM TIER 1 AND TIER 2 CAPITAL							
							(amount in thousands)	
1.1	Investments in equity and other regulatory capital of majority owned securities or other financial subsidiaries not consolidated in the balance sheet	13,176.6	13,095.5	1,514.2	11,265.9	-	315.5	81.1
1.2	Significant minority investments in banking, securities and other financial entities (para 1.1. scope of Application)	4,638.0	3,309.7	1,869.8	1,439.9	-	-	1,328.3
1.3	Equity holdings (majority or significant minority) in an insurance subsidiary (para 1.1. scope of Application)	125.9	125.9	-	125.9	-	-	-
1.4	Significant minority and majority investments in commercial entities exceeding 15% of bank's capital	421.1	121.1	-	121.1	-	-	300.0
1.5	Securitization exposure subject to deduction (para 4.3.1 of instructions)	-	-	-	-	-	-	-
1.6	Others	-	-	-	-	-	-	-
		434.8	75.0	-	75.0	-	-	359.8
1.7	Total Deductible Items to be deducted 50% from Tier 1 capital and 50% from Tier 2 capital	18,796.4	16,727.2	3,383.9	13,027.8	-	315.5	2,069.2

Group-wise Composition of Banks March 31, 2008

2006	2007	2008	Mar-09
A. Public Sector Com. Banks (4) National Bank of Pakistan First Women Bank Ltd. The Bank of Khyber The Bank of Punjab	A. Public Sector Com. Banks (4) National Bank of Pakistan First Women Bank Ltd. The Bank of Khyber The Bank of Punjab	A. Public Sector Com. Banks (4) National Bank of Pakistan First Women Bank Ltd. The Bank of Khyber The Bank of Punjab	A. Public Sector Com. Banks (4) National Bank of Pakistan First Women Bank Ltd. The Bank of Khyber The Bank of Punjab
B. Local Private Banks (24) Askari Commercial Bank Ltd. Bank Alfalah Ltd. Bank AL Habib Ltd. Mybank Ltd. Faysal Bank Ltd. Habib Metropolitan Bank Ltd. KASB Bank Ltd. Prime Commercial Bank Ltd. Saudi Pak Commercial Bank Ltd PICIC Commercial Bank Ltd. Soneri Bank Ltd. Standard Chartered Bank (Pakistan) MCB Bank Ltd. Allied Bank Ltd. United Bank Ltd. Meezan Bank Ltd. NIB Bank Ltd. Crescent Commercial Bank Ltd. Habib Bank Ltd. Atlas Bank Ltd.. Arif Habib Rupali Bank Ltd. Dubai Islamic Bank Pakistan Ltd. BankIslami Pakistan Ltd. JS Bank Ltd.	B. Local Private Banks (26) Askari Bank Ltd. Bank Alfalah Ltd. Bank AL Habib Ltd. Mybank Ltd. Faysal Bank Ltd. Habib Metropolitan Bank Ltd. KASB Bank Ltd. ABN AMRO Bank (Pakistan) Ltd 1 Saudi Pak Commercial Bank Ltd PICIC Commercial Bank Ltd. Soneri Bank Ltd. Standard Chartered Bank (Pakistan) MCB Bank Ltd. Allied Bank Ltd. United Bank Ltd. Meezan Bank Ltd. NIB Bank Ltd. Crescent Commercial Bank Ltd. Habib Bank Ltd. Atlas Bank Ltd.. Arif Habib Bank Ltd. Dubai Islamic Bank Pakistan Ltd. BankIslami Pakistan Ltd. JS Bank Ltd. Emirates Global Islamic Bank Ltd. Dawood Islamic Bank Ltd	B. Local Private Banks (25) Askari Bank Ltd. Bank Alfalah Ltd. Bank AL Habib Ltd. Mybank Ltd. Faysal Bank Ltd. Habib Metropolitan Bank Ltd. KASB Bank Ltd. The Royal Bank of Scotland Ltd 1 Saudi Pak Commercial Bank Ltd Soneri Bank Ltd. Standard Chartered Bank (Pakistan) MCB Bank Ltd. Allied Bank Ltd. United Bank Ltd. Meezan Bank Ltd. NIB Bank Ltd. SAMBANK Bank Ltd. Habib Bank Ltd. Atlas Bank Ltd.. Arif Habib Bank Ltd. Dubai Islamic Bank Pakistan Ltd. BankIslami Pakistan Ltd. JS Bank Ltd. Emirates Global Islamic Bank Ltd. Dawood Islamic Bank Ltd	B. Local Private Banks (25) Askari Bank Ltd. Bank Alfalah Ltd. Bank AL Habib Ltd. Mybank Ltd. Faysal Bank Ltd. Habib Metropolitan Bank Ltd. KASB Bank Ltd. The Royal Bank of Scotland Ltd 1 Saudi Pak Commercial Bank Ltd Soneri Bank Ltd. Standard Chartered Bank (Pakistan) MCB Bank Ltd. Allied Bank Ltd. United Bank Ltd. Meezan Bank Ltd. NIB Bank Ltd. SAMBANK Bank Ltd. Habib Bank Ltd. Atlas Bank Ltd.. Arif Habib Bank Ltd. Dubai Islamic Bank Pakistan Ltd. BankIslami Pakistan Ltd. JS Bank Ltd. Emirates Global Islamic Bank Ltd. Dawood Islamic Bank Ltd
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D. Specialized Banks (4) Zarai Taraqiati Bank Ltd. Industrial Development Bank of Punjab Provincial Co-operative Bank SME Bank Ltd.	D. Specialized Banks (4) Zarai Taraqiati Bank Ltd. Industrial Development Bank of Punjab Provincial Co-operative Bank SME Bank Ltd.	D. Specialized Banks (4) Zarai Taraqiati Bank Ltd. Industrial Development Bank of Punjab Provincial Co-operative Bank SME Bank Ltd.	D. Specialized Banks (4) Zarai Taraqiati Bank Ltd. Industrial Development Bank of Punjab Provincial Co-operative Bank SME Bank Ltd.
All Commercial Banks (35) Include A + B + C	All Commercial Banks (36) Include A + B + C	All Commercial Banks (36) Include A + B + C	All Commercial Banks (36) Include A + B + C
All Banks (39) Include A + B + C + D	All Banks (40) Include A + B + C + D	All Banks (40) Include A + B + C + D	All Banks (40) Include A + B + C + D

List of Abbreviations

ADD	Authorized Derivatives Dealer
ADR	Advances to Deposits Ratio
BIA	Basic Indicator Approach
bps	Basis Points
CAR	Capital Adequacy Ratio
CB	Commercial Bank
CCF	Credit Conversion Factor
CCS	Cross Country Swaps
CDR	Credit to Deposit Ratio
CPI	Consumer Price Index
CPV	Credit Portfolio View
CRM	Credit Risk Mitigants
CRR	Cash Reserve Requirements
CRWA	Credit Risk Weighted Amounts
CY	Calendar Year
DFIs	Development Finance Institutions
ERF	Export Refinance
EURIBOR	Euro Interbank Offered Rate
EXR	Exchange Rate
FB	Foreign Bank
FDBR	Financial Derivatives Business Regulations
FDR	Financing to Deposits Ratio
FR	Forward Rate Agreements
FSV	Forced Sale Value
GDP	Gross Domestic Product
Govt.	Government
HTM	Held-to-Maturity
IBIs	Islamic Banking Institutions
IRS	Interest Rate Swaps
KIBOR	Karachi Interbank Offered Rate
KSE	Karachi Stock Exchange
LIBOR	London Interbank Offered Rate
LoLR	Lender of Last Resort
LPB	Local Private Bank
LR	Interest Rate
MCR	Minimum Capital Requirement
MRWA	Market Risk Weighted Amounts
MTB	Market Treasury Bill
NII	Net Interest Income
NMI	Non-Market Maker Financial Institution
NOP	Net Open Position
NPF	Non Performing Finance
NPL	Non Performing Loan

NPLR	Loan Infection Ratio
NSS	National Saving Scheme
OMO	Open Market Operation
ORWA	Operational Risk Weighted Amounts
OTC	Over the Counter
PAT	Profit After Tax
PIB	Pakistan Investment Bond
PICIC	Pakistan industrial Credit and Investment Corporation
PKR	Pak Rupee
PSCB	Public Sector Commercial Bank
PTCs	Participation Term Certificates
QoQ	Quarter on Quarter
QPR	Quarterly Performance Review
QRC	Quarterly Report of Condition
ROA	Return on Asset
ROE	Return on Equity
RSA	Rate Sensitive Assets
RSL	Rate Sensitive Liabilities
RWA	Risk Weighted Assets
SA	Standardized approach
SB	Specialized Bank
SBP	State Bank of Pakistan
SECP	Securities and Exchange Commission of Pakistan
SLR	Statutory Liquidity Requirements
SME	Small and Medium Enterprise
TFCs	Term Finance Certificates
USD	United States Dollar
YoY	Year on Year

Glossary

Capital Adequacy Ratio is the amount of risk-based capital as a percent of risk-weighted assets.

Coefficient of Variance The coefficient of variance is the ratio of Standard Deviation to Arithmetic Mean. The coefficient is a useful statistical tool for comparing the degree of volatility of more than one data sets when their means are significantly different from each other.

Consumer Financing means any financing allowed to individuals for meeting their personal, family or household needs. The facilities categorized as Consumer Financing include credit cards, auto loans, housing finance, consumer durables and personal loans.

Corporate means and includes public limited companies and such entities, which do not come under the definition of SME.

Credit risk arises from the potential that a borrower or counter-party will fail to perform an obligation or repay a loan.

Discount rate is the rate at which SBP provides three-day repo facility to banks, acting as the lender of last resort.

Duration (Macaulay's Duration) is a time weighted present value measure of the cash flow of a loan or security that takes into account the amount and timing of all promised interest and principal payments associated with that loan or security. It shows how the price of a bond is likely to react to different interest rate environments. A bond's price is a function of its coupon, maturity and yield.

Force Sale Value (FSV) means the value that can currently be obtained by selling the mortgaged / pledged assets in a forced / distressed sale conditions. This value fully reflects the possibility of price fluctuations.

GAP is the term commonly used to describe the rupee volume of the interest-rate sensitive assets versus interest-rate sensitive liabilities mismatch for a specific time frame; often expressed as a percentage of total assets.

Gross income is the net interest income (before provisions) plus non-interest income;

the income available to cover the operating expenses.

Interbank rates are the two-way quotes namely bid and offer rates quoted in interbank market are called as interbank rates.

Interest rate risk is the exposure of an institution's financial condition to adverse movement in interest rates, whether domestic or worldwide. The primary source of interest rate risk is difference in timing of the re-pricing of bank's assets, liabilities and off-balance sheet instruments.

Intermediation cost is the administrative expenses divided by the average deposits and borrowings.

Liquid assets are the assets that are easily and cheaply turned into cash – notably cash and short-term securities. It includes cash and balances with banks, call money lending, lending under repo and investment in government securities.

Liquidity risk is the risk that the bank will be unable to accommodate decreases in liabilities or to fund increases in assets. The liquidity represents the bank's ability to efficiently and economically accommodate decreases in deposits and to fund increases in loan demand without negatively affecting its earnings.

Market risk is the risk that changes in the market rates and prices will impair an obligor's ability to perform under the contract negotiated between the parties. Market risk reflects the degree to which changes in interest rates, foreign exchange rates, and equity prices can adversely affect the earnings of a bank.

Net interest income is the total interest income less total interest expense. This residual amount represents most of the income available to cover expenses other than the interest expense.

Net Interest Margin (NIM) is the net interest income as a percent of average earning assets.

Net loans are the loans net of provision held for NPLs.

Net Non-Performing Loans (NPLs) is the value of non-performing loans minus provision for loan losses.

Net NPLs to net loans means net NPLs as a percent of net loans. It shows the degree of loans infection after making adjustment for the provision held.

Non-Performing Loans (NPLs) are loans and advances whose mark-up/interest or principal is overdue by 90 days or more from the due date.

NPLs to loans ratio/Infection ratio stands for NPLs as a percent of gross loans.

Paid-up capital is the equity amount actually paid by the shareholders to a company for acquiring its shares.

Rate Sensitive Assets (RSA) are assets susceptible to interest rate movements; that will be re-priced or will have a new interest rate associated with them over the forthcoming planning period.

Repricing risk arises from timing differences in the maturity of fixed rate and the repricing of floating rates as applied to banks' assets, liabilities and off-balance sheet positions

Return on assets measures the operating performance of an institution. It is the widely used indicator of earning and is calculated as net profit as percentage of average assets.

Return on equity is a measure that indicates the earning power of equity and is calculated as net income available for common stockholders to average equity

Risk weighted Assets: Total risk weighted assets of a bank would comprise two broad categories: credit risk-weighted assets and market risk-weighted assets. Credit risk weighted assets are calculated from the adjusted value of funded risk assets i.e. on balance sheet assets and non-funded risk exposures i.e. off-balance sheet item. On the other hand for market risk-weighted assets, first the capital charge for market risk is calculated and then on the basis of this charge amount the value of Market Risk Weighted Assets is derived.

Secondary market is a market in which securities are traded following the time of their original issue.

SME means an entity, ideally not a public limited company, which does not employ more than 250 persons (if it is manufacturing/ service concern) and 50 persons (if it is trading concern) and also fulfils the following criteria of either 'a' and 'c' or 'b' and 'c' as relevant:

(a) A trading / service concern with total assets at cost excluding land and building upto Rs50 million.

(b) A manufacturing concern with total assets at cost excluding land and building upto Rs100 million.

(c) Any concern (trading, service or manufacturing) with net sales not exceeding Rs300 million as per latest financial statements.

Tier-I capital: The risk based capital system divides capital into two tiers- core capital (Tier I) and supplementary capital (Tier II and Tier III). Tier 1 capital includes fully paid up capital, balance in share premium account, reserve for issue of bonus shares, general reserves as disclosed on the balance-sheet and un-appropriated /un-remitted profit (net of accumulated losses, if any).

Tier-II capital or Supplementary Capital (Tier II & III) is limited to 100 percent of core capital (Tier I). Tier II includes; general provisions or general reserves for loan losses, revaluation reserves, exchange translation reserves, undisclosed reserves and subordinated debt.

Tier-III capital consists of short-term subordinated debt and is solely held for the purpose of meeting a proportion of the capital requirements for market risks.

Yield risk is the risk that arises out of the changes in interest rates on a bond or security when calculated as that rate of interest, which, if applied uniformly to future time periods sets the discounted value of future bond coupon and principal payments equal to the current market price of the bond.

Yield curve risk materializes when unanticipated shifts have an adverse effect on the bank's income or underlying economic value