The Team

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List of Abbreviations

CAR	Capital Adequacy Ratio
CB	Commercial Bank
CDR	Credit to Deposit Ratio
CRR	Cash Reserve Requirement
CY	Calendar Year
FB	Foreign Bank
HTM	Held-to-Maturity
IB	Islamic Bank
IBB	Islamic Bank Branch
IBI	Islamic Banking Institution
LPB	Local Private Bank
MCR	Minimum Capital Requirement
MTB	Market Treasury Bill
NII	Net Interest Income
NOP	Net Open Position
NPF	Non Performing Finance
NPL	Non Performing Loan
NSS	National Saving Scheme
OMO	Open Market Operation
PIB	Pakistan Investment Bond
PSCB	Public Sector Commercial Bank
ROA	Return on Asset
ROE	Return on Equity
RSA	Rate Sensitive Asset
RSL	Rate Sensitive Liability
RWA	Risk Weighted Asset
SBP	State Bank of Pakistan
SB	Specialized Bank
SLR	Statutory Liquidity Requirement
SME	Small and Medium Enterprise

Glossary

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

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.

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.

Contents

Quarterly Performance Review of the Banking System
September 2007 [1]

Overview

The banking system has further consolidated its resilience against adverse shocks during September 2007 quarter on the back of strong capital base. In addition, continued healthy profitability of the banking system helped to absorb the additional burden of incremental non-performing loans (NPLs) during the quarter. The Return on Assets (ROA) remained healthy at 2.0 percent, whereas, the Return on Equity (ROE) of the banking system marginally declined to 20.0 percent, as compared to 20.6 percent in Jun-07 at the back large increase in paid up capital of the banks.

The increment in NPLs seems to be one of the consequences of extra ordinary expansion of the private sector credit during last few years, primarily with the intention to explore new areas. The credit expansion appeared to be decelerating in the beginning of CY07; it touched its highest level of Rs 2.5 trillion in Jun-07 and came down marginally in Sep-07 quarter. The NPLs have increased in absolute terms as well as a percentage of total loans mainly due to slowdown in credit and fresh NPLs in consumer loans. The decline in advances also led to a reduction in the assets of the banking system in the quarter under review. Consequently, the banks preferred to change their asset portfolio mix and redirected their funds towards investment component.

The banks continued to receive fresh funds in the form of capital and deposits. While the former was due to strong profitability and minimum capital requirement (MCR) policy, the latter was primarily due to external

[1] The review is based on the data mainly taken from the Quarterly Reports of Condition and Annual Audited Accounts submitted by the banks. It covers their global operations, unless otherwise mentioned. The banks have been divided into four groups namely, Public Sector Commercial Banks (PSCBs), Local Private Banks (LPBs), Foreign Banks (FBs) and Specialized Banks (SBs). PSCBs include two nationalized commercial banks and two provincial banks, whereas LPBs consist of four privatized banks and twenty two domestic private banks. The composition of these four groups has been given at Annex-IV. The performance of the overall banking system, particularly these groups of banks, has been evaluated using the financial soundness indicators.

inflows especially workers' remittances, which were even higher in Sep-07 quarter than the ample amount witnessed in earlier quarters.

The strong deposit inflows along with decline in advances and rise in investment in relatively liquid assets led to improve liquidity position of the banking system. Though the liquidity risk of the banking system improved, the credit risk raises a sign of concern emanating from incremental NPLs. Specifically, NPLs to Advances ratio (both gross and net) deteriorated slightly in Sep-07 quarter. Moreover, the market risks remained subdued as the interest rate and exchange rate showed only tiny movements.

Given the seasonal nature of asset growth, it is expected that the credit growth would regain momentum in the Dec-07 quarter and banking sector would continue to demonstrate year-on-year growth trend experienced in last few years. The liquidity available with the banks provides sufficient room to improve on their earning assets. Further, it is also expected that all the banks would meet MCR and CAR via mergers, acquisition transactions and right issues as well as through other equity instruments.

Executive Summary

Assets and Funding Structure

The assets of the banking system witnessed modest decline during Sep-07 quarter, though the Jan-Sep 2007 cumulative increase in the assets of the banking system remained above the increase recorded in the corresponding periods of CY04-CY06.

The slowdown in loans and advances continued, as a result, their share in the total assets decreased marginally to 50.4 percent in Sep-07 quarter, bringing the Jan-Sep 07 cumulative decline to 5.4 percentage points. In fact, the loans and advances component has decreased in absolute terms; due to persistent deceleration in credit to the private sector primarily coming from slowdown in consumer loans and decrease in working capital and commodity financing. On the other hand investment portfolio of the banking system continued to enhance its weight during Sep-07 quarter. The share of investment in total assets rose by 2.8 percentage points during Sep-

07 quarter, reached 26.6 percent; bringing the cumulative Jan-Sep 07 increase to 7.3 percentage points.

Though the deposits of the banking system witnessed a comparatively modest rise in Sep-07 quarter, the cumulative Jan-Sep 07 rise was a phenomenal Rs 489.4 billion, significantly higher than the increase recorded in preceding years. The deposits component was well supplemented by the equity support, which raised its share to 10.2 percent in Sep-07 quarter, up 0.8 percentage points during CY07 so far. The capital of the banking system stood at Rs 499.3 billion in Sep-07, up by approximately 25 percent during Jan-Sep 07. More importantly, nearly 60 percent of the capital rise came in the form of paid up (assigned) capital, primarily to meet the increased MCR. The healthy profits also supplemented the growing net assets of the banking system.

Solvency

Solvency position of the banking system gained further strength on the back of healthy profits and fresh capital injection. The qualifying risk-based capital of the banking system increased by Rs19.1 billion to Rs438.2 billion in Sep-07 quarter. The core capital increased not only in absolute terms but also in terms of share in total capital due to decline in supplementary capital. The CAR of all banks rose to 13.6 percent in Sep-07 as compared to 13.3 percent in Jun-07.

Total risk weighted assets growth slowed down, however, RWA to total assets increased by 2 percentage points to 65.9 percent in Sep-07 quarter. This can be explained by decline in total assets of the banking system as well as compositional shift away from risky asset i.e. from advances to investment.

Profitability

Overall, operating performance of the banking system further strengthened during Jun-07 quarter. Both the core and non-core income contributed to the healthy profits. The before and after tax profits reached Rs102.8 billion and Rs68.4 billion respectively in Sep-07 and constitute 83 percent and 81 percent of CY06 full-year profits. After tax ROA maintained the last quarter level of 2 percent. Further, ROE declined marginally by 0.6 percent to 20 percent.

The profit & loss composition of commercial banks (CBs) has witnessed a slight change. The share of net interest income in the gross income, which registered a slight decline of 2.5 percent to 70.5 percent in Sep-07, was counterbalanced by the corresponding rise in the other non-interest income by 2.6 percent to 12.5 percent in Sep-07. Particularly, other non-interest income almost doubled during the quarter from Rs13 billion to Rs25.9 billion in Sep-07.

The slow increase in interest income may be attributed to declining interest rate spread between the weighted average rates on incremental loans and fresh deposits. The spread dropped down to 4.4 percent in Sep-07 from 5.0 percent in Jun-07. The return on fresh deposits increased to 6.0 percent as compare to 5.3 percent in Jun-07.

Credit Risk

The fast credit growth in the previous years has resulted in higher Credit Risk of the banking system during the Sep-07 quarter. Despite the decline in loans of the banking system, total non-performing loans (NPLs) further increased by Rs13.5 billion to Rs201 billion in Sep-07 quarter. Major increase occurred in the initial categories of NPLs i.e. other assets especially mentioned (OAEM) and substandard, which in turn brought about higher increase in the net NPLs (increased by Rs12 billion to Rs57 billion). Further, most of the asset quality ratios of the banking system deteriorated marginally on overall basis, among various categories of the banks and various segments of the loans during the Sep-07 quarter.

Market Risk

Risk of re-pricing was contained as the re-pricing GAPs were largely within the acceptable range. Re-pricing gaps in all three time buckets were within +/-10 percent of total assets in local private banks (LPBs) and foreign banks (FBs). However SBs and PSCBs have significant positive gaps in 3-month to one-year bucket. Maturity mismatches have raised the yield curve risk for the banks. Though the increase in the interest rate remained gradual, comparatively higher increase in the short-term interest rate during Jan-Nov 07 has flattened the yield curve.

For the exchange rate risk, Pak rupee against US dollar remained broadly stable and hovered around Rupee 60.60 to 60.8 during Sep–07 quarter. Subsequent to Sep-07, the pressure was seen on the rupee; consequently the rupee depreciated and touched the level of Rs62 per USD in Dec-07 in the interbank market. Foreign exchange exposure of the banks seemed at mild level. Net Open position (NOP) of the bank though was negative in the end September, largely remained positive December onwards.

Liquidity Risk

Liquidity position of the banking system improved further during Sep-07 quarter. Main contributing factors include easing of loans to deposit ratio (from 63.9 in Jun-07 to 63.5 percent in Sep-07) and continuous shift of share of advances to investments. With major portion of investments in the government securities held in available for sale (AFS) and held for trading (HFT) categories further substantiated the improved liquidity of the banking system.

Maturity GAPs however remained a source of concern. Although the overall gap between assets and liabilities as percentage of total assets remained below +/-10 percent, however, individual groups showed significant negative gaps in 3-month maturity bucket that may raise liquidity concerns for the banks.

Islamic Banking

Islamic Banking has come a long way since 2002 when it started with a single bank and has now grown to six full-fledged Islamic Banks (IBs) and 12 conventional banks operating Islamic Banking branches. As a result of continuous growth over the last 5 years, size of Islamic banking system has grown to 3.6 percent of the total assets of the banking sector in September, 2007. Major development regarding the Islamic banking sector has been the shift from the Murahaba financing, which is still the major type of financing, to other modes like Diminishing Musharika.

With improving asset quality and profitability coupled with capital adequacy above the required ratio and expanding branch network, the IBIs appear to be firmly placed to gain further share in the banking system.

Resilience of the Banking System-Sensitivity Analysis

Fortifying capital base has lent greater resilience to the banking system against the adverse shocks. Capital of all banks can fairly absorb the impact of a shock of 10 percent in increase in NPLs. None of the groups would experience a fall in its CAR to below 8 percent. However, the impact of an increase in NPLs equivalent to 10 percent of consumer loans would be higher; individually, 4 banks holding a share of 11 percent in the assets of banking system would experience a decline in their CAR to below 8 percent under this sensitivity test.

The impact of interest rate, exchange rate and equity price shocks can also be well absorbed by the healthy capital. Increased liquidity position has improved the resilience of the banking system towards liquidity shocks.

2. Assets and Funding Structure

Figre 2.1: Cumulative Assets Growth

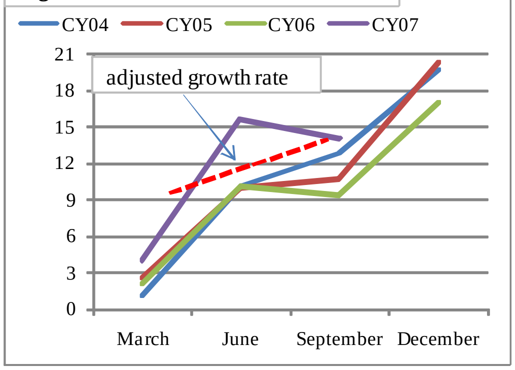
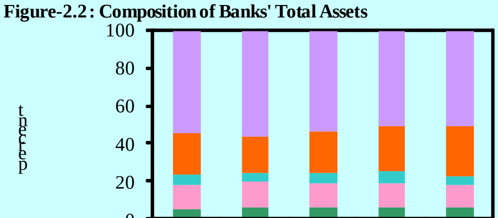


Figure-2.2: Composition of Banks' Total Assets



	CY05	CY06	Mar-07	Jun-07	Sep-07
Advances	54.4	55.8	53.2	50.5	50.4
Investments	21.9	19.2	22.0	23.8	26.6
Lending to FIs	5.8	4.9	5.2	6.4	4.4
Cash & Balances	12.8	13.7	13.2	13.2	12.0
Other Assets	5.2	6.4	6.5	6.2	6.6

The assets of the banking system witnessed a decline during Sep-07 quarter, though the Jan-Sep 07 cumulative increase and growth remained higher than the increase recorded in the corresponding periods of CY04-CY06. The slowdown in September quarter exhibits cyclical behaviour prevalent in the corresponding quarters of the previous years (**Figure 2.1**). The quarterly growth in assets is -1.4 percent, however, year to date growth in total assets is 14.0 percent which is considerably higher than the growth recorded in corresponding periods of last few years (**Figure 2.1**).

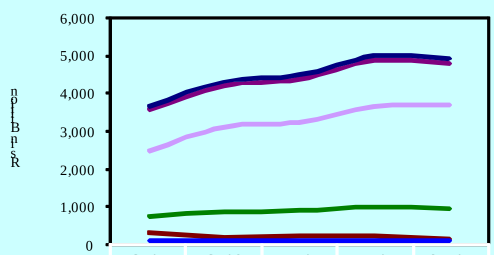
The asset structure continued to shift away from loans and advances during Sep-07 quarter (see **Figure 2.2**). Specifically, the share of loans and advances in total assets of the banking system further reduced by 0.1 percentage points to 50.4 percent in Sep-07 quarter, bringing the Jan-Sep 07 cumulative decline to 5.4 percentage points. In fact, the loans and advances component has decreased in absolute term during Sep-07 quarter first time in last five years. The persistent slowdown in credit to the private sector has ultimately resulted in an absolute decline, primarily arising from a reduction in working capital for commodity finance and slowdown in consumer loans.[2]

[2] See details in ***Advances*** section.

While the loan component continues to loose its weight in total assets during Jan-Sep 07, the lending to financial institutions and cash & balances also lost their share to investment in Sept-07 quarter. Specifically the investments continued to enhance their share in assets which rose by 2.8 percentage points to 26.6 percent during Sep-07 quarter; bringing the cumulative Jan-Sep 07 increase to 7.4 percentage points (**Figure-2.2**). Though deceleration in private sector credit is one of the reasons for banks growing investment portfolio, the continuous surge in deposits and enhanced capital base added further liquidity of the banking system that led the banks to change their portfolio mix.

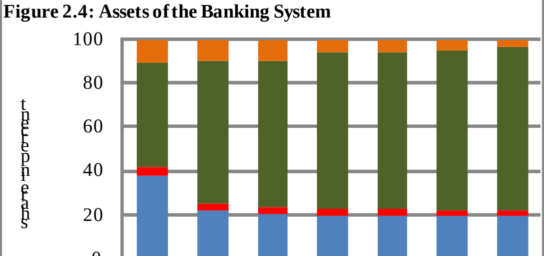
The banking group-wise composition of assets reveals that LPBs have increased their share to 75.1 percent from 72.9 percent in the last quarter (see **Figure 2.3** and **Figure 2.4**). This increase is a result of merger of ABN Amro Bank into locally incorporated bank, consequently the share of FBs decreased in total assets of the banking system. The share of PSCBs which was almost stagnant for the last two quarters declined marginally (by 0.4 percent) to 19.1 percent in the current quarter due to decrease in assets of the largest PSCB.

Figure-2.3: Total Assets of Banking System



	CY05	CY06	Mar-07	Jun-07	Sep-07
PSCBs	724	836	864	964	934
LPBs	2,483	3,102	3,215	3,611	3,666
FBs	339	224	256	254	169
CBs	3,547	4,162	4,334	4,829	4,769
SBs	113	120	118	123	115
All	3,660	4,282	4,453	4,952	4,884

Figure 2.4: Assets of the Banking System



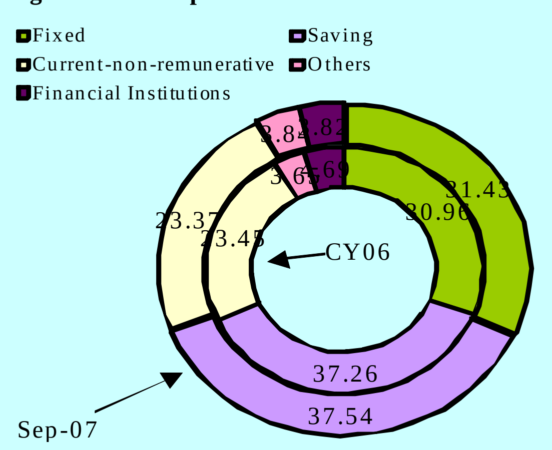
	CY03	CY04	CY05	CY06	Mar-07	Jun-07	Sep-07
FBs	10.7	10.0	9.3	5.2	5.7	5.1	3.5
LPBs	47.7	65.1	67.8	72.4	72.2	72.9	75.1
SBs	3.9	3.5	3.1	2.8	2.7	2.5	2.4
PSCBs	37.7	21.5	19.8	19.5	19.4	19.5	19.1

Though the asset distribution of banking system remained highly skewed towards top 5 banks; banking concentration continued its declining trend. Particularly, the share of five big-banks declined by 0.5 percent to 50.6 percent in Sep-07 quarter and by 2 percent as compared to corresponding quarter of the last year. Number of banks having 2 percent or more of banking assets increased to 15 from 13 in Jun-07 quarter.

Deposits and other accounts', the largest component of the banking system funds, witnessed a seasonal modest rise in Sep-07 quarter, bringing the cumulative Jan-Sep 07 rise to phenomenal Rs 489.4 billion. As a matter of fact, the deposits have been growing very rapidly over the last four years; and Jan-Sep 07 deposits increase (in each quarter) was by a long way higher than preceding three years' performance. The huge external inflows like workers' remittances and public and private sector debt and equity flows were the main contributors in steady deposit growth. This strong rise contributed 81.4 percent in assets accumulation of the banking system during first nine months of CY07. As a result, the stock of deposits enhanced its share in total assets of the banking system by 1.2 percentage points to 75.6 percent in Sep-07 quarter.

Within the categories of deposits, the savings deposits remained the largest component, followed by fixed deposits and current (non-remunerative) deposits. The Sep-07 quarter did not see a considerable change in the composition, however, the trend visible over last couple of years continued in Sep-07 quarter. Specifically, saving deposits have been replaced gradually by fixed deposits; and in Sep-07 quarter the share of fixed deposits increased by 0.9 percentage points to 31.4 percent at the cost of shares of savings deposits as well as deposits from financial institutions (see **Figure:-2.5**).

Figure-2.5: Deposits Structure



The ***Capital***, which is the second largest source of assets funding, recorded a marginal growth (0.2 percent) in Sep-07 quarter. Nevertheless, the Jan-Sep

07 cumulative increase remained higher than the increase recorded in the corresponding periods of earlier years. The capital of the banking system reached Rs499.3 billion in Sep-07, up by nearly Rs100.6 billion from CY06.

Despite the modest increase in capital during the quarter under review, the policy of MCR has resulted in growing share of capital in funding total assets of the banking system. Specifically, the assets backed by capital entered into double digit (10.2 percent) in Sep-07, first time in years from as low as 4.8 percent in CY02. More importantly, paid up capital contributed most of the capital augmentation during the current quarter as well as in Jan-Sep 07 in contrast to Jan-Sep 06 where most of the increase was contributed by revaluation surplus, reserves and unappropriate profit.

The ***Borrowings*** of the banking system witnessed a turnaround in Sep-07 quarter, recorded a substantial decline of Rs 103 billion after recording a massive increase of Rs 97.5 billion in Jun-07 quarter. As a result, the share of borrowings in funding of total assets dropped by 2 percentage points in Sep-07 quarter.

A further analysis of banking system borrowings unveils that both secured and unsecured components witnessed decline in Sep-07 quarter. In secured borrowings, the banks paid back Rs 29.3 billion to the SBP, which they availed under refinance of EFS; and reduced the borrowings under repo agreements by Rs 51.3 billion. The banks also decreased the unsecured call borrowings by Rs 18.7 billion in Sep-07 quarter. It is important to note that the share of secured borrowings in total borrowings increased significantly during Jan-Sep 07 period; raised its share by 5 percentage points to 89.1 percent in Sep-07.

The ***Advances*** (net) of the banking system witnessed a slowdown in CY07 so far, after showing substantial expansion during CY03-CY06 (27.2 percent per annum). In fact, of the three quarters of CY07, the March and September quarter recorded decline of Rs 20.5 billion and Rs 39.5 billion respectively. However, the Jun-07 quarter increase was large enough to bring the Jan-Sep 07 cumulative increase to Rs 70.2 billion, only 32.6 percent of increase in advances recorded in the comparative period of CY06. The lower increase in advances resulted in a sharp decline of its share in total assets by 5.4 percentage points during first nine months of CY07 to 50.4 percent in Sep-07.

A breakup of advances data[3] witnessed slowdown across the board as well as absolute decline in some sectors both during Sep-07 quarter and Jan-Sep 07 (see **Table 2.1**). Specifically, the absolute decline was recorded in working capital loans of the corporate sector and commodity financing, followed by small decline in other personal loans. An important point to note here is that corporate sector borrowings for trade finance increased significantly during the quarter as well as in Jan-Sep 07 period. The corporate sector borrowing for fixed investment increased marginally in Sep-07 quarter; however the volume of increase during Jan-Sep 07 is significant.

Table 2.1: End-use of Advances (net)

Amount in billion Rs, share in percent

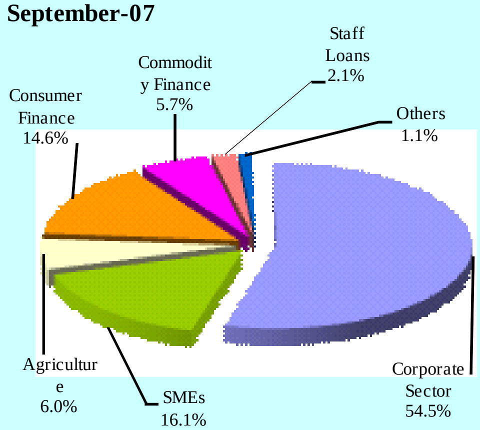
	Dec-06		Mar-07		Jun-07		Sep-07	
	Amount	Share	Amount	Share	Amount	Share	Amount	Share
Fixed Investment	**503.4**	**21.0**	**529.1**	**22.3**	**534.4**	**21.6**	**546.1**	**22.3**
Corporate Sector:	461.6	19.2	482.2	20.3	490.0	19.8	499.0	20.4
SMEs:	41.8	1.7	46.9	2.0	44.4	1.8	47.1	1.9
Trade Finance	**336.4**	**14.0**	**373.6**	**15.7**	**369.6**	**14.9**	**393.9**	**16.1**
Corporate Sector:	278.3	11.6	311.4	13.1	309.5	12.5	329.9	13.5
SMEs:	58.1	2.4	62.2	2.6	60.1	2.4	64.0	2.6
Working Capital*	**1,161.4**	**48.4**	**1,062.1**	**44.7**	**1,135.6**	**45.8**	**1,074.5**	**43.9**
Corporate Sector:	539.2	22.5	512.0	21.6	543.8	21.9	504.3	20.6
SMEs:	308.4	12.8	278.0	11.7	278.3	11.2	283.7	11.6
Agriculture	141.9	5.9	140.5	5.9	144.3	5.8	148.1	6.0
Commodity Financing	171.9	7.2	131.6	5.5	169.2	6.8	138.4	5.7
Consumer Finance:	**325.2**	**13.5**	**333.9**	**14.1**	**354.4**	**14.3**	**356.6**	**14.6**
Credit Cards	39.2	1.6	41.3	1.7	44.5	1.8	47.5	1.9
Auto Loans	104.1	4.3	105.1	4.4	107.6	4.3	111.4	4.5
Consumer Durable	1.3	0.1	4.1	0.2	1.0	0.0	1.4	0.1
Mortgage Loan	49.2	2.1	52.0	2.2	58.1	2.3	60.6	2.5
Other personal Loans	131.3	5.5	131.4	5.5	143.3	5.8	135.8	5.5
Staff Loans	**48.0**	**2.0**	**48.0**	**2.0**	**48.9**	**2.0**	**50.6**	**2.1**
Housing Finance	32.7	1.4	33.9	1.4	34.7	1.4	35.7	1.5
Others	15.2	0.6	14.1	0.6	14.2	0.6	14.8	0.6
Others	**26.4**	**1.1**	**27.7**	**1.2**	**35.9**	**1.4**	**26.4**	**1.1**
Total	**2,400.8**	**100.0**	**2,374.4**	**100.0**	**2,478.8**	**100.0**	**2,448.1**	**100.0**

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

[3] This section is based on banks domestic operations only.

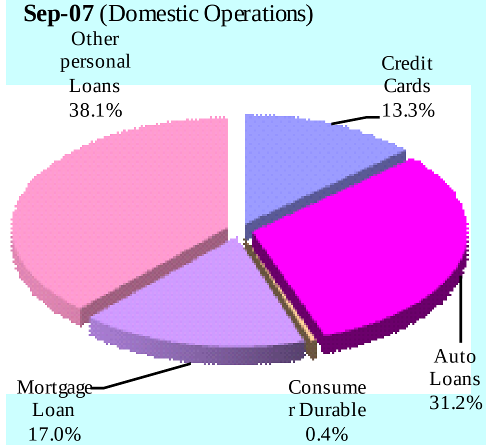
In relative terms, there was a visible shift in the composition of end-use of the banking system advances. Specifically, the year 2007 so far witnessed a decline in the share of working capital loans which was largely captured by fixed investment loans, trade finance and consumer finance. In terms of user/segment of the advances, the corporate sector is still the biggest borrower of banking system followed by SME sector and consumer finance. Commodity finance and other unspecified sector lost their shares in total advances whereas rest of the sectors inched up their shares in Sep-07 quarter. SME sector increased its share by 0.68 percentage points whereas corporate sector and consumer finance inched up their shares by 0.27 percentage points each (see **Figure 2.6**).

Figure-2.6 : Loans by Type of Borrowers-September-07



Consumer finance continued to decelerate in Sep-07 quarter. A break up of consumer finance data reveals that while the loans in 'other personal loans' category declined in absolute term to Rs 135.8 billion from 143.3 billion during Sep-07 quarter, the loans under remaining categories did show tiny increases. Consequently, the share of all consumer products in overall consumer loans increased except other personal loans. Nonetheless, other personal loans remained the largest consumer finance product followed by unchanged sequence of other products as seen in Jun-07 quarter (see **Figure 2.7**).

Figure-: 2.7: Composition of Consumer Loans-Sep-07 (Domestic Operations)



Investment **(*net*)**, the second largest component of the assets of the banking system next to the advances (net) saw a sharp increase both in terms of absolute volume as well as share in total assets. Specifically, the investment recorded an increase of Rs476.1 billion, nearly 80 percent of assets increase during Jan-Sep 07. Comparing it with advances, the increase in investment was about nine times of the increase in the advances in this period. The (net) investment growth rate in CY07 so far is phenomenal 57.6 percent, not seen in last many years. These changes resulted in growing share of investment in total assets; reached 26.6 percent in Sep-07, from below 20 percent in CY06.

Figure-: 2.8: Break up of Investments - Sep-07

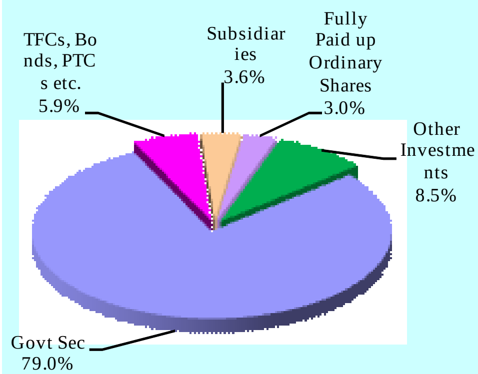
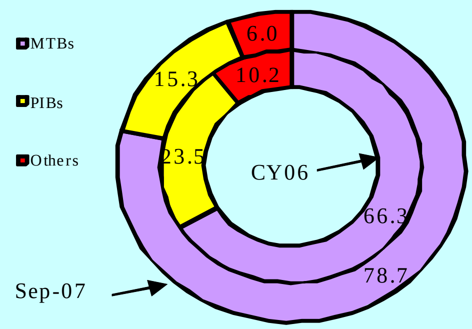


Figure-2.9: Break up of Federal Govt. Securities



The investment data breakdown reveals that in Sep-07, 79 percent of the banks' investment is in federal government securities, mostly in short-term marketable treasury bills (MTBs) followed by long-term Pakistan Investment Bonds (PIBs). It is important to note that the investment in federal government securities increased by Rs 396.7 billion during Jan-Sep 07, followed by other investment (Rs 44.7 billion) and investment in subsidiaries and associated undertakings (Rs 30.8 billion) (see **Figure 2.8**).

A break up of investment in federal government securities shows that the addition came almost entirely from MTBs followed by a tiny contribution from PIBs (see **Figure 2.9**). Consequently, the share of MTBs in government securities increased to 78.7 percent in Sep-07 from 66.3

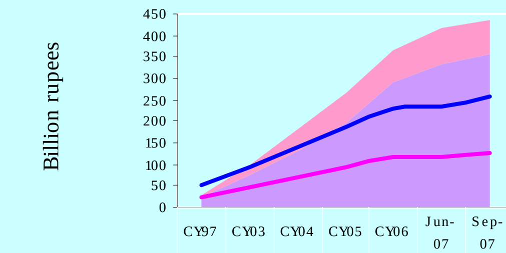
percent in CY06. Moreover, there was substantial increase in other investment during the period under review.

3 Financial Soundness of the Banking System

3.1 Solvency

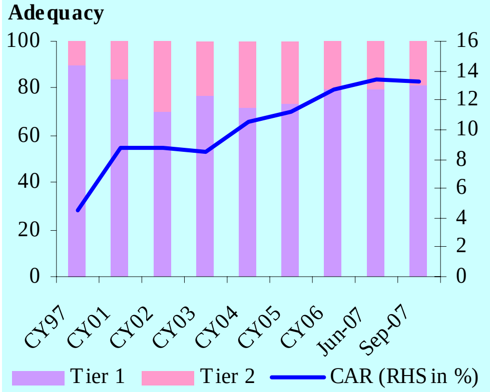
Solvency position of the banking system gained further strength on the back of healthy profits and fresh capital injection. The qualifying risk-based capital of the banking system increased by Rs19.1 billion to Rs438.2 billion in Sep-07 quarter. More importantly, the core capital being the mainstay of banks' capital increased by Rs23 billion. However, the supplementary capital declined by 4.6 percent during the quarter under review (see **Figure-3.1.1**) due to decrease in general provisions, retirements of subordinated debt and revaluation of reserves. As a result, the share of core capital in total capital increased to 81.6 percent (see **Figure-3.1.2**).

Figure-3.1.1: Risk-based Capital Position



	CY97	CY03	CY04	CY05	CY06	Jun-07	Sep-07
Supplementary Capital	2.9	23.3	50.8	69.7	76.2	84.6	80.7
Core Capital	25.4	77.0	131.7	195.3	288.3	334.5	357.5
Required Core	25.0	47.3	69.6	94.2	115.2	118.3	128.7
Required Total	50.0	94.7	139.3	188.3	230.5	236.55	257.37

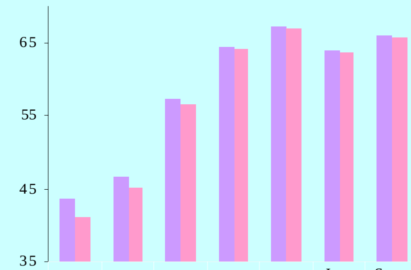
Figure:-3.1.2 Capital Structure and Capital Adequacy



Total risk-weighted assets of the banking system increased by 1.8 percent in Sep-07 as compare to an increase of 7 percent in Jun-07 quarter. The slower increase in risk weighted assets may be explained by decline in total assets of the banking system as well as compositional shift away from risky asset i.e. from advances to investment. The shift in asset mix has also resulted in increasing the RWA as a percentage of total assets by 2 percentage points to 65.9 percent in Sept-07 quarter (see **Figure: 3.1.3**).

The capital grew at relatively higher pace as compared to increase in risk weighted assets, which further strengthened the solvency of the banking system. Interestingly all the capital indicators registered increase in the current quarter as compared to last quarter. Specifically, the CAR rose to 13.6 percent in Sep-07 as compared to 13.3 percent in Jun-07 (see **Table 3.1.1**). Core Capital to RWAs ratio also strengthened to 11.1 percent from 10.6 percent. This implies that both ratios exceed the generally acceptable benchmarks for well-capitalized banks.

Figure-3.1.3: RWA to Total Assets



	CY97	CY03	CY04	CY05	CY06	Jun-07	Sep-07
All Banks	43.5	46.5	57.2	64.3	67.3	63.9	65.9
Comm. Banks	41.1	45.2	56.6	64.1	67.0	63.7	65.7

Table-3.1.1: Capital Adequacy Indicators

Percent	CY97	CY03	CY04	CY05	CY06	Jun-07	Sep-07
CAR							
PSCBs	(1.3)	11.0	13.4	14.5	15.2	16.2	17.1
LPBs	11.9	9.0	10.1	10.6	12.7	13.2	13.4
FBs	14.6	23.0	17.4	16.4	15.0	14.0	14.9
CBs	6.0	11.1	11.4	11.9	13.3	13.8	14.2
SBs	(6.2)	(28.2)	(9.0)	(7.7)	(8.3)	(7.3)	(8.0)
All banks	4.5	8.5	10.5	11.3	12.7	13.3	13.6
Tier 1 Capital to RWA							
PSCBs	(2.0)	8.2	8.6	8.8	11.1	11.9	13.1
LPBs	11.4	7.0	7.5	8.3	10.4	10.9	11.3
FBs	14.4	23.0	17.1	16.1	14.3	13.3	14.2
CBs	5.5	9.1	8.6	9.1	10.7	11.2	11.8
SBs	(6.3)	(28.7)	(15.0)	(13.6)	(13.3)	(12.7)	(13.4)
All banks	4.1	6.5	7.6	8.3	10.0	10.6	11.1
Capital to Total Assets							
PSCBs	0.3	6.1	8.7	12.6	12.2	12.4	13.4
LPBs	4.9	5.3	6.5	7.0	9.2	9.8	9.9
FBs	7.9	9.9	8.9	9.5	10.1	9.6	11.2
CBs	3.1	6.1	7.2	8.4	9.9	10.3	10.6
SBs	8.8	(10.0)	(9.4)	(8.1)	(8.0)	(6.2)	(7.5)
All banks	3.5	5.5	6.7	7.9	9.4	9.9	10.2

Group-wise, CAR of PSCBs remained the highest at 17.1 percent followed by the FBs at 14.9 percent, both registering an increase of 0.9 percentage points as compared to June-07 quarter. Core Capital to RWAs of FBs remained the highest at 14.2 percent.

The other key solvency ratios also witnessed improvement during the quarter, Capital to total assets ratio increased to 10.2 percent in Sep-07 from 9.9 percent in Jun-07 (see **Table-3.1.1**).

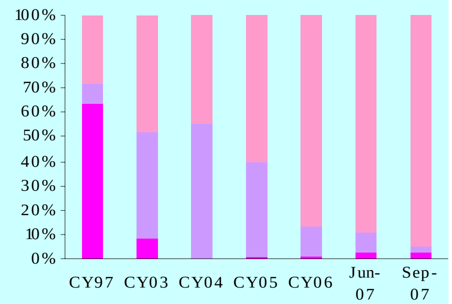
The disaggregated analysis shows that out of 40 banks, well-capitalized banks i.e., the banks with CAR of more than 10 percent increased to 36 from 35 in Jun-07 (see **Table-3.1.2**). Of the remaining 4, one bank has CAR above 8 percent. In fact, the share of well-capitalized banks has increased from 89.2 percent in Jun-07 to 94.9 percent in Sep-07 (see **Figure-3.1.4**).

As regards the compliance with minimum capital requirement, 34 out of 40 banks are meeting this requirement (this includes 5 foreign banks, which are allowed to keep Rs2 billion instead of Rs3 billion as capital). Of the remaining, 4 banks are under process of restructuring/ privatization and the rest are going through merger process and have been given short extensions to meet MCR by end of the current year.

Table-3.1.2: Distribution of Banks by CAR

	Total	Below 8%	8 to 10 %	10 to 15 %	Over 15 %
CY02	40	4	4	9	23
CY03	40	4	10	5	21
CY04	38	1	13	9	15
CY05	39	2	7	13	17
CY06	39	3	4	15	17
Jun-07	41	2	4	17	18
Sep-07	40	3	1	19	17

Figure-3.1.4: Banks' Market Share by CAR

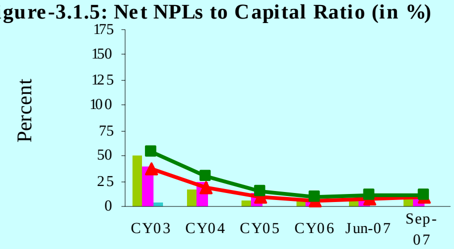


	CY97	CY03	CY04	CY05	CY06	Jun-07	Sep-07
10 percent and above	28.0	48.2	44.5	60.5	86.7	89.2	94.9
8 to 10 percent	8.7	43.8	55.1	38.8	12.1	8.2	2.4
Below 8 percent	63.3	8.0	0.4	0.7	1.2	2.6	2.7

Owing to relatively faster increase in NPLs, Net NPLs to Capital ratio however increased to 11.4 percent from 10.7 percent in Jun-07 (see **Figure 3.1.5**). Group wise position shows that PSCBs witnessed greater increase by 1.8 percentage points whereas this ratio for FBs remained negative due to excess provisioning.

Conclusively, aided by strong profits and capital injections to meet the enhanced minimum capital requirement, the banks witnessed strengthening of their solvency position. However, the banks need to keep check on quality of assets so as to ensure sustained profitability and solvency profile.

Figure-3.1.5: Net NPLs to Capital Ratio (in %)



	CY03	CY04	CY05	CY06	Jun-07	Sep-07
PSCBs	50.0	16.2	5.4	6.4	5.4	7.2
LPBs	39.1	24.3	12.7	7.1	9.6	9.6
FBs	3.2	(0.2)	-3.0	(5.1)	(5.0)	(4.3)
SBs	-	-	-	-	-	-
CBs	36.9	19.0	8.8	6.2	7.8	8.5
All Banks	54.4	29.2	14.1	9.7	10.7	11.4

3.2 Profitability

The pace of strong earnings remained intact during Sep-07 quarter. Both the core and non-core income contributed to the healthy profits. The before and after tax profits reached Rs102.8 billion and Rs68.4 billion respectively in Sep-07 as compare to Rs90.3 billion and Rs61.7 billion respectively in the corresponding period of last year (see **Table 3.2.1**).

Group-wise, LPBs remained the highest contributors to before and after tax profits, which increased to Rs73.5 billion and Rs48.7 billion respectively as compare to Rs56.5 billion and Rs 38.1 billion in the corresponding period of the last year. While the merger of one of the FBs into LPBs increased the profits of LPBs, it also resulted in the lower profitability of FBs. PSCBs remained the other key contributor with before and after tax profits of Rs27.4 billion and Rs19.2 billion respectively as compare to Rs16.7 billion and Rs11.1 billion in Jun-07 quarter. The PSCBs have earned Rs4.3 billion as dividend income during the quarter ended Sep-07 which was just Rs0.3 billion in Jun-07.

Table-3.2.1: Profitability of Banking System

(Billion Rs)	CY03	CY04	CY05	CY06	Mar-07	Jun-07	Sep-07
Profit before tax							
PSCBs	16.1	14.2	22.8	31.5	7.8	16.7	27.4
LPBs	23.8	31.0	60.5	85.6	24.4	49.1	73.5
FBs	7.1	7.2	11.6	6.3	2.1	2.8	2.5
CBs	47.0	52.4	94.9	123.5	34.3	68.6	103.4
SBs	(3.3)	(0.4)	(1.1)	0.1	(1.3)	(0.1)	(0.5)
All Banks	43.7	52.0	93.8	123.6	33.1	68.5	102.8
Profit after tax							
PSCBs	9.4	8.0	15.5	21.2	5.2	11.1	19.2
LPBs	14.8	21.8	41.1	59.1	16.4	32.8	48.7
FBs	4.2	5.8	8.0	4.3	1.3	1.6	1.2
CBs	28.4	35.6	64.6	84.6	22.9	45.5	69.2
SBs	(3.7)	(0.9)	(1.3)	(0.5)	(1.3)	(0.1)	(0.8)
All Banks	24.7	34.7	63.3	84.1	21.6	45.4	68.4

Table-3.2.2: Profitability Indicators

(Percent)	CY03	CY04	CY05	CY06	Mar-07	Jun-07	Sep-07
After Tax ROA							
PSCBs	1.0	1.3	2.2	2.7	2.4	2.5	2.9
LPBs	1.4	1.2	1.8	2.1	2.1	2.0	2.0
FBs	1.5	2.0	2.5	1.5	2.1	1.3	1.0
CBs	1.2	1.3	2.0	2.2	2.2	2.1	2.1
SBs	(3.7)	(0.8)	(1.2)	(0.4)	(4.2)	0.6	(0.9)
All Banks	1.0	1.2	1.9	2.1	2.0	2.0	2.0
After Tax ROE (based on Equity plus Surplus on Revaluation)							
PSCBs	17.3	17.2	20.9	21.7	19.8	20.3	22.6
LPBs	25.8	20.2	27.2	25.3	22.1	20.7	19.6
FBs	14.8	21.5	27.1	15.6	22.0	13.2	8.8
CBs	20.3	19.6	25.4	23.7	21.5	20.2	19.9
SBs	-	-	-	-	-	-	-
All Banks	20.0	20.3	25.8	24.2	20.6	20.6	20.0

The performance of banking system in terms of ROA and ROE after tax remained largely on the last quarter's level. Specifically, the ROA maintained at 2 percent whereas ROE declined slightly to 20 percent from

20.6 percent in Jun-07 (see **Table 3.2.2**). It is worthy to note that paid up capital increased by Rs30.8 billion in Sep-07 quarter, which substantially raised the equity base of the banks to Rs499.3 billion.

The Group-wise analysis shows that PSCBs have shown remarkable increase both in before and after tax ROA. The slight deterioration in profitability indicators of LPBs in Jun-07 quarter improved during Sep-07 quarter. The after tax ROA and ROE of LPBs have reached 2.0 percent and 19.6 percent in Sep-07 from 2.0 percent and 20.7 percent in Jun-07. However, after tax ROA and ROE of FBs declined as one large foreign bank shifted to LPBs category.

During the quarter under review, the profit & loss composition of CBs witnessed a slight change as the share of net interest income in the gross income has slightly declined to 70.5 percent in Sep-07 (see **Figure 3.2.1**). However, such a decline was counterbalanced by the corresponding rise in the other non-interest income to 12.5 percent in Sep-07. The share of fee-based and currency dealing income in the gross income slightly

Figure-3.2.1: CBs' P&L Structure

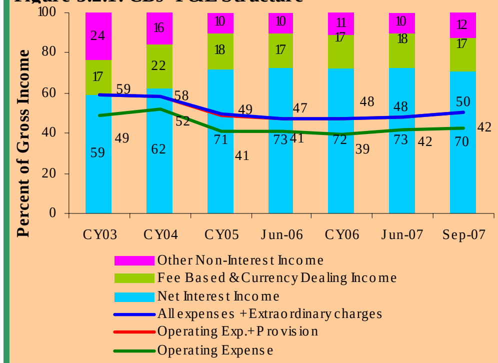


Figure-3.2.2: Operating Exp. to Gross Income

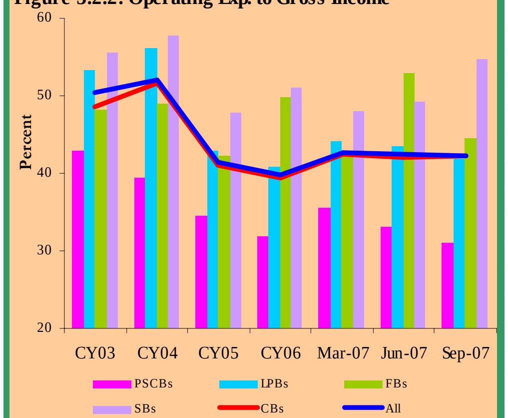
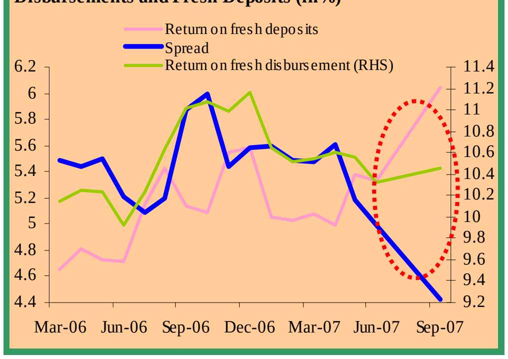


Figure-3.2.3: Weighted Average Rates for Fresh Disbursements and Fresh Deposits (in%)



dropped by 0.4 percentage points to 17.1 percent in Sep-07 which was at the level of Rs35.4 billion in Sep-07. The other non-interest income also doubled from Rs13 billion in Jun-07 to Rs25.9 billion in Sep-07. Further, the increased provisioning raised the share of operating expenses and provisions in the gross income by 2 percent.

On the expense side, share of operating expenses in gross income remained at the same level. However, PSCBs have shown some improvement as their operating expense to gross income ratio decreased by 2 percent to 31 percent in Sep-07 whereas FBs showed marginal deterioration as their ratio has increased to 55 percent in Sep-07 from 53 percent in Jun-07 (see **Figure 3.2.2**).

The analysis of core income reveals that CBs' net mark up/interest income kept increasing though at a slower rate. It has increased by 52 percent to Rs146.3 billion in Sep-07 from Rs96.1 billion in Jun-07. This increase may be attributed to higher cost of deposits during the quarter. It also suggests that deposit rates are also responding to the increasing lending rates. The declining interest rate spread between the weighted average rates of returns on incremental loans and fresh deposits strongly favour this viewpoint. The spread has dropped to 4.4 percent in Sep-07 from 5.0 percent in Jun-07 (see **Figure:-3.2.3**). The return on fresh deposits has increased to 6.0 percent from 5.3 percent in Jun-07.

The further analysis of ROA shows that 23 banks have ROA one percent and above and their market share have also increased from 82.8 percent in Jun-07 to 85.4 percent in Sep-07 (see **Table 3.2.3**). However the number of banks having ROA 0.5 percent to 1.0 percent dropped to 4 in Sep-07 from 6 in Jun-07. Further, banks having less than 0 percent ROA have increased from 7 to 9 in Sep-07. Most of the banks in this category are either recently established banks or where change of management has taken place for meeting the shortfall in MCR. Most of

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

	CY05		CY06		Mar-07		Jun-07		Sep-07	
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	7	4.6	7	2.0	9	2.5
0 to 0.5	4	2.8	3	1.8	6	3.4	5	4.1	4	7.6
0.5 to 1	2	7	6	9.9	4	7.5	6	11.1	4	4.5
1.0 to 1.5	5	4	5	9.6	5	6.7	5	6.8	5	12.0
1.5 and Over	21	82.7	19	76.6	18	77.8	18	76.0	18	73.4

these institutions are in expansionary phase, where the administrative expenses are usually high, thus lower ROA.

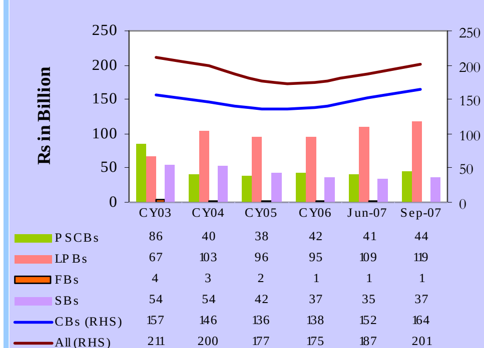
The recent mergers and acquisition transactions, technological advancement and improvement in quality of human resource of the banking sector have positively impacted the profitability of the banking industry.

4. Risk Assessment of the Banking System

4.1 Credit Risk

Credit risk of the banking system experienced a marginal increase during the Sep-07 quarter. Although loans of the banking system experienced a decline of Rs39 billion to Rs2,459 billion in Sep-07 quarter, total non-performing loans (NPLs) of the banking system witnessed an increase of Rs13.5 billion to Rs201 billion in Sep-07 quarter mainly due to an increase in the NPLs of commercial banks (see **Figure: - 4.1.1**). This increase in NPLs was not unexpected on the back of aggressive credit growth in the last few years.

Figure:-4.1.1 NPLs of Banking System



Group-wise position shows that LPBs, holding the largest pie in loans portfolio, were the major contributors to increase in NPLs. Low cash recoveries and recognition of large number of NPLs in OAEM and Sub-standard categories by one of the larger private banks were the key factors behind this increase.

Figure:-4.1.2 Category-wise Breakup of NPLs

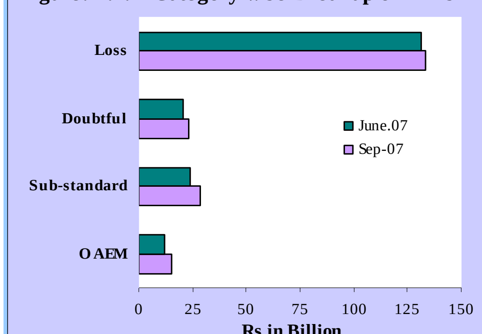
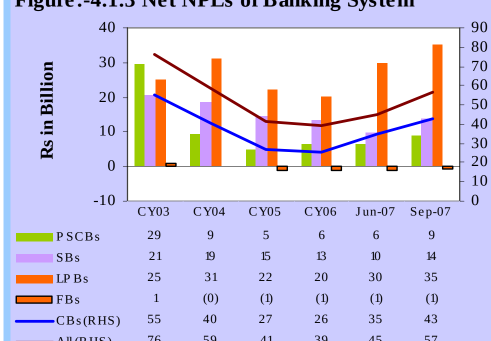


Figure:-4.1.3 Net NPLs of Banking System



The category-wise break-up of NPLs shows that increase has been witnessed in all the four categories. In absolute terms, significant increase has been seen in initial categories i.e. OAEM and sub-standard.

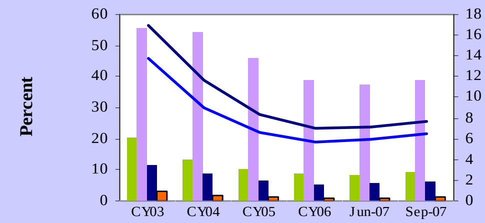
However, the share of loss category is still quite high, with the amount of NPLs of Rs133 billion (see **Figure:- 4.1.2**).

Moreover, Net NPLs of the banking system witnessed an increase of Rs12 billion to Rs57 billion in Sep-07 mainly due to increase in fresh stock of NPLs, which requires no or lesser provisions (see **Figure:-4.1.3**). All the categories of bank except FBs have shared this increase. FBs remained successful to proactively manage their credit risk by making provisions more than the regulatory requirement.

The rise in NPLs during the quarter stressed the assets quality ratios. Precisely the NPLs to Loans ratio (gross) for all banks has increased by 0.6 percent to 7.7 percent in Sep-07 quarter; importantly, the CBs experienced slightly lesser increase of 0.5 percent to 6.5 percent (see **Figure:- 4.1.4**)..

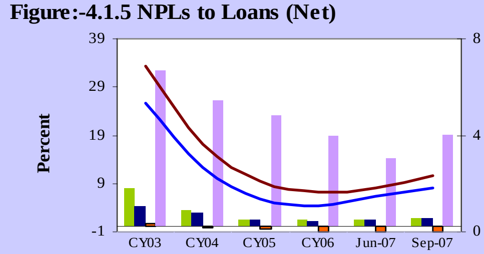
Similarly, NPLs to loans ratio (net) slightly deteriorated, as it moved up to 2.3 percent in Sep-07 from 1.8 percent in Jun-07 (see **Figure:-4.1.5**). The major increase was seen in SBs category. The slowdown in credit during current quarter also adversely impacted the NPLs to Loans ratio (net).

Figure:-4.1.4 NPLs to Loans (Gross)



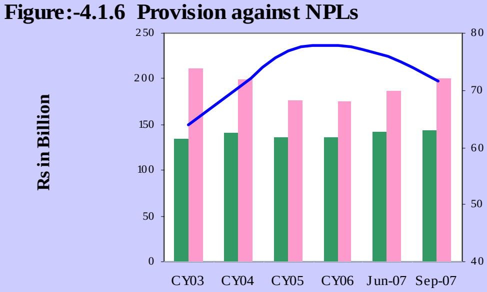
	CY03	CY04	CY05	CY06	Jun-07	Sep-07
PSCBs	20	13	10	9	8.5	9.1
SBs	56	54	46	39	37.7	38.9
LPBs	11	9	6	5	5.7	6.1
FBs	3	2	1	1	1.1	1.2
CBs (RHS)	14	9	7	6	6.0	6.5
All (RHS)	17	12	8	7	7.1	7.7

Figure:-4.1.5 NPLs to Loans (Net)



	CY03	CY04	CY05	CY06	Jun-07	Sep-07
PSCBs	8	3	1	2	1.4	2.0
LPBs	5	3	2	1	1.6	1.9
FBs	1	(0)	(1)	(1)	(1.0)	(1.0)
SBs	33	26	23	19	14.4	19.2
CBs (RHS)	5	3	1	1	1.5	1.8
All (RHS)	7	4	2	2	1.8	2.3

Figure:-4.1.6 Provision against NPLs



	CY03	CY04	CY05	CY06	Jun-07	Sep-07
Provision	135	141	136	137	142	144
NPLs	211	200	177	175	187	201
Provision to NPLs (RHS)	64	70	77	78	76	72

The increase in NPLs by Rs13.5 billion during Sep-07 along with a lesser increase in provision (by Rs2.0 billion) adversely impacted the coverage ratio (see **Figure:-4.1.6**). Specifically, the coverage ratio declined to 72 percent in Sep-07 from 76.0 percent in Jun-07. Further analysis of the coverage ratios shows that FBs have the highest coverage ratio of 183 percent followed by PSCBs (80 percent), LPBs (71 percent) and SBs (62.6 percent) in Sep-07.

Disaggregated analysis reveals that the increase in NPLs has been shared by all of the loan segments (see **Table:-4.1.1**). In absolute terms, SMEs witnessed the highest increase (Rs4.0 billion), followed by corporate (Rs3.6 billion), agriculture (Rs3.0 billion) and consumer finance (Rs2.9 billion). NPLs to loans ratio of agriculture sector remained the highest among all the segments followed by SMEs, corporate and consumer segment. Specifically, the Consumer finance NPLs to loans ratio of increased by 0.8 percent to 4.4 percent in Sep-07. This increase was basically contributed by the auto loans, which registered a substantial increase of 1.5 percent to 3.9 percent followed by mortgage loans, which registered an increase of 1.4 percent to 4.3 percent in Sep-07.

Table: 4.1.1 Segmentwise Infection of Loans Portfolio

(Domestic Operations) **(in %)**

Sector	CBs		SBs		All	
	Sep-07	Jun-07	Sep-07	Jun-07	Sep-07	Jun-07
Corporate	6.9	6.6	100.0	98.4	7.2	6.9
SMEs	8.5	7.7	84.6	85.3	10.4	9.7
Agriculture	11.6	7.8	31.7	29.6	22.0	19.3
Consumers	4.4	3.6	10.0	19.8	4.4	3.6
Credit Cards	6.3	6.6	-	-	6.3	6.6
Auto Loans	3.8	2.4	14.8	14.0	3.9	2.4
Consumer Durables	46.4	14.8	27.2	25.4	45.3	15.7
Mortgage Loans	4.3	2.9	-	-	4.3	2.9
Others	3.8	3.8	-	-	3.8	3.8
Commodity Finance	0.9	0.8	-	-	0.9	0.8
Staff Loans	0.8	0.8	0.1	0.1	0.8	0.8
Others	3.6	3.6	15.4	14.4	3.8	3.7
Total	6.4	5.8	39.0	37.7	7.7	7.0

Overall, loan portfolio of the banking system experienced deterioration during the quarter, which though undesirable but not unpredicted. Aggressive loan growth during the past few years not only lent a hand to this deterioration but also made the asset quality management a bit challenging for the banks in near future.

4.2 Market Risk

Of the three market risk factors, ***interest rate risk*** carries a greater significance in terms of explaining the market risk of banking system in Pakistan.

During Sep-07 quarter, interest rates witnessed an overall increase almost in all the short and medium term maturities. Major rise was noticed in short-term maturities. However, interest rate on long-term maturities of over 5 years actually declined from its Dec-06 level. Comparatively higher increase in the short-term interest rate during Jan-Nov 07 has flattened the yield curve (see **Figure:-4.2.1**). However, since the movement in the yield curve, on the average, was less than half a percentage point, the concern on the interest rate risk remains subdued.

Risk of re-pricing was contained since the overall re-pricing GAPs[4] were largely within the acceptable range. In all three time buckets (up to 3 months, 3-12 months, and over 1 year buckets), re-pricing gaps were within +/-10 percent of total assets in commercial banks (see **Figure:-4.2.2**). Group wise analysis shows that FBs and PSCBs have negative gaps of 12 percent in up to 3 months bucket but significant positive gaps in 3-12 months and over 1 year buckets.

Figure-4.2.1: Shift in Yield Curve

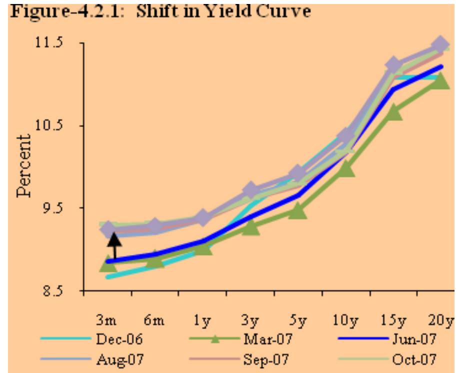


Figure:-4.2.2 GAP b/w Rate Sensitive Assets and Laibilities to Total Assets (in %) Sep-07

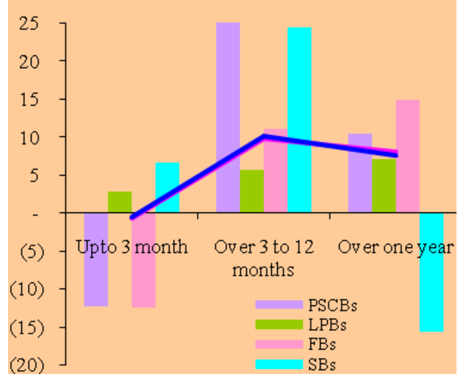
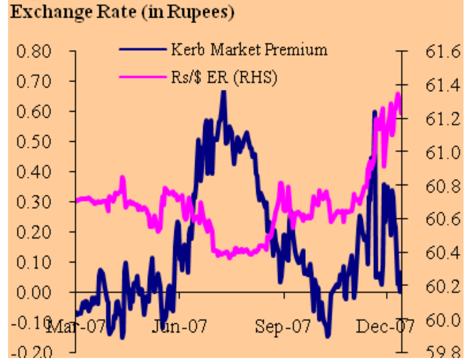


Figure: 4.2.3 Kerb Market Premiums and Rs/$ Exchange Rate (in Rupees)



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[4] GAPs between rate sensitive assets and rate sensitive liabilities

However, LPBs which constitutes about 75 percent of the total banking assets had the re-pricing GAPs well below +/-10 percent of their total assets in all 3 buckets.

For the ***exchange rate risk***, Pak rupee remained broadly stable against the dollar in past few years, and it hovered around Rupee 60.6 to 60.8 per USD during Sep-07 quarter (see **Figure:- 4.2.3**). Subsequent to Sep-07, the rupee came under pressure; and depreciated to the level of Rs 62 per USD in Dec-07 in the interbank market. Foreign exchange exposure of the banks seemed at mild level. Net Open position (NOP) of the banks though was negative in the end September, largely remained positive in December onwards period (see **Figure 4.2.4**).

The ***equity exposure*** of the banking system (which includes investments both in listed and unlisted stocks) has increased from Rs33.2 billion to Rs38.1 billion in Sep-07 quarter. This is also reflected in the overall exposure of the banks in equities, which as a percentage of their net assets increased to 7.6 percent in Sep-07 from 6.8 per cent in Jun-07.

Figure:-4.2.4 NOP of All Banks (in Million $)

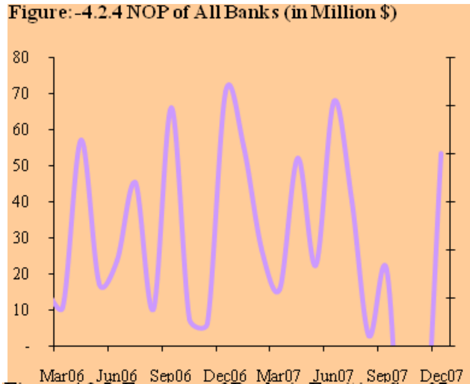


Figure-4.2.5: Exposure of Banks in Equities-Sep-07

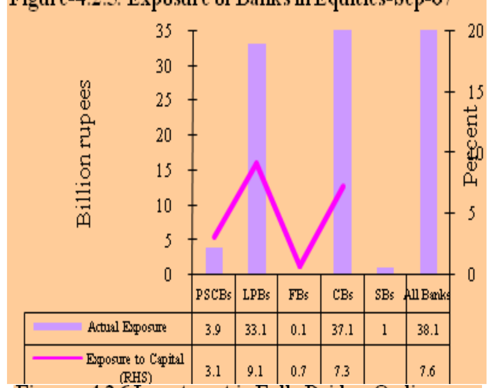
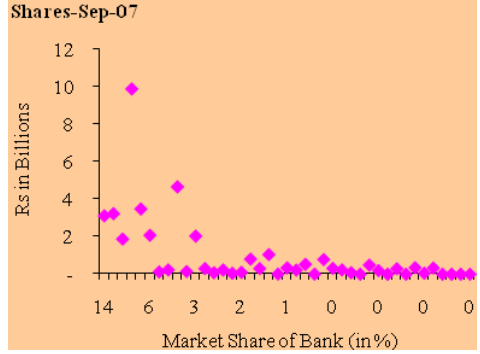


Figure:-4.2.6 Investment in Fully Paid up Ordinary Shares-Sep-07



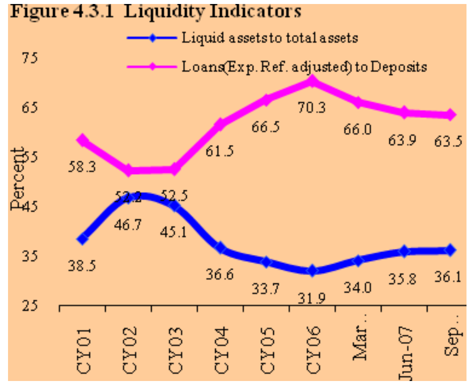
According to group-wise analysis, none of the banking groups has exposure over 9.1 percent in terms of capital. LPBs group, being the largest banking segment, holds about 87 percent of the total equity exposure of the banking system. As per the disaggregated analysis, top 5 banks in terms of total assets of the banking system share almost 57 percent of the total equity investment. In terms of capital, the exposure of almost all of the banks is fairly within the acceptable limits.

Summing up, increase in the interest rates during the quarter might have increased market risk for a few banks that have significant re-pricing GAPs. Inflationary expectations and trade imbalances are also putting pressure on the rupee and slackening of credit off take has mildly exposed the banks to the risks associated with the investments.

4.3 Liquidity Risk

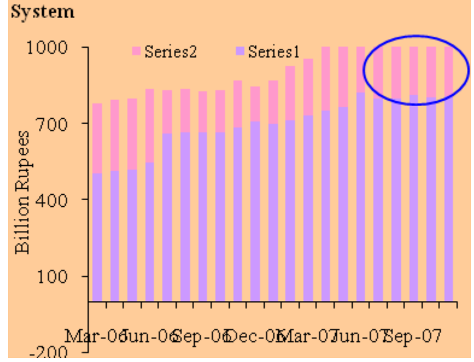
During the Sep-07 quarter, liquidity position of the banking system experienced further ease as the liquid assets in terms of total assets increased to 36.1 percent from 35.8 percent. Loans to deposit ratio also experienced slight ease to 63.5 percent from 63.9 percent in Jun-07 (see **Figure:-4.3.1**).

Figure 4.3.1 Liquidity Indicators



In fact, the compositional shift in the asset-mix of the banking system improved the liquidity profile of the banking system. Specifically, an increase in the investments by Rs121 billion, (which also raised its share in total assets to 26.6 percent) provided additional liquidity during the quarter. This is also reflected in the higher excess liquid reserves maintained by the banking system in addition to the statutory liquidity requirement (see **Figure:-4.3.2**). Surplus liquidity of the banking system has found its way in government securities, as evident from excess liquid reserves maintained over and above the statutory liquidity requirement by the banks.

Figure: -4.3.2 Excess Reserves Held by the Banking System



Market based liquidity increased as a significant share of the government securities have been categorized under HFT and AFS categories. Investment in HFT and AFS securities increased to 85 percent as compared to 83 percent in June-07. An important point to note is that around 96 percent of MTBs have been placed under tradable categories (see **Figure:-4.3.3**).

Maturity-mismatches i.e. GAPs between the maturity of asset and liabilities, another indicator of liquidity, were largely within the acceptable range. As of Sep-07, the overall gap between assets and liabilities as percentage of total assets in commercial banks remained below 10 percent in all three maturities buckets.[5] LPBs which constituted about 75 percent of the total banking assets were also within the acceptable range in the three maturity buckets. In 3 month maturity band; FBs and PSCBs recorded significant negative gaps; thereby raising a concern for short-term liquidity for these banks (see **Figure:-4.3.4**). This large negative gap may also be attributable to the nature of deposit structure as the large amount of deposits generally fall in the near-term buckets.

Figure:-4.3.3 MTBs of the Banking System Sep-07

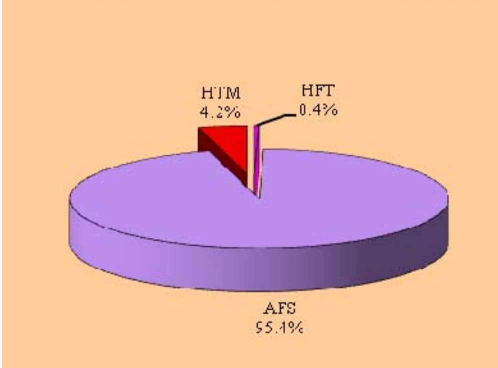
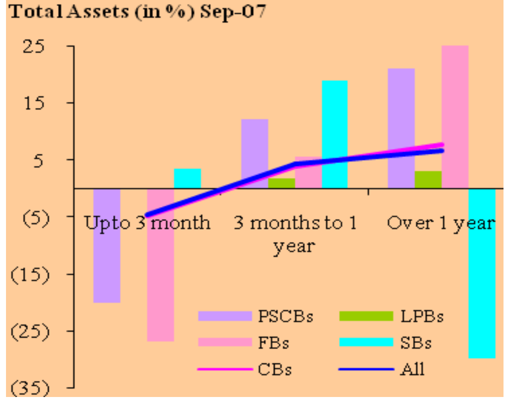


Figure:-4.3.4 Maturity GAP (Assets - Liabilities) to Total Assets (in %) Sep-07



Summing up, liquidity of the banking system has increased during Sep-07 quarter. A compositional shift away from advances to investments added to the liquidity profile of the banking system.

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5 Up to 3 months, 3-12 months, and over 1 year.

5. Performance of Islamic Banking

Islamic Banking has come a long way since 2002 when it started with a single bank. As of Sep-07, the system constitutes six full-fledged Islamic Banks (IBs) having 132 branches and 12 conventional banks are operating 63 Islamic banking branches (see **Table-5.1**). The size of Islamic Banking System grew by 11.7 percent during the quarter against a reduction of 1.4 percent of all banks. The balance sheet has grown by 49 percent since CY06 (see **Table-5.2**). Consequently the share of IBs has increased from 3.2 percent in Jun-07 to 3.6 percent in Sep-07.

Table-5.1: Islamic Banking Participants

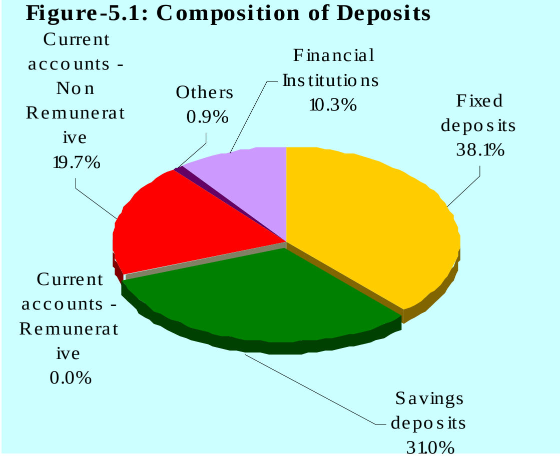
	CY02	CY03	CY04	CY05	CY06	June 07	Sept 07
No. of Islamic Banks (IBs)	1	1	2	2	4	6	6
No. of Branches	6	10	23	37	93	109	132
No. of conventional banks operating Islamic Banking Branches	-	3	7	9	12	12	12
No. of Islamic Banking Branches (IBBs)	-	7	21	33	57	58	63

Table-5.2: Sources and Uses of Funds (Billion rupees)

	CY03	CY04	CY05	CY06	Jun 07	Sept 07
SOURCES						
Deposits	8.4	30.2	49.9	83.7	108.3	124.4
Borrowings	1.9	6.6	9.0	10.8	14.3	14.7
Capital & other funds	2.0	5.1	7.8	16.3	25.2	26.1
Other liabilities	0.6	2.3	4.7	8.4	11.1	12.5
	12.9	**44.1**	**71.5**	**119.3**	**159.0**	**177.7**
USES:						
Financing	8.7	27.5	45.8	65.6	78.8	88.3
Investments	1.2	2.0	1.9	7.3	11.5	25.5
Cash, bank balance, placements	2.0	11.9	19.3	31.4	53.2	46.3
Other assets	1.0	2.7	4.5	15.0	15.5	17.6
	12.9	**44.1**	**71.5**	**119.3**	**159.0**	**177.7**

A review of the channels of funds reveals that the deposits continue to dominate the sources of funds for the Islamic Banking System. The share of deposits increased from 68 percent in Jun-07 to 70 percent in Sep-07. Investments increased by 121 percent whereas Cash, bank balance and placements experienced a decline of 12.9 percent

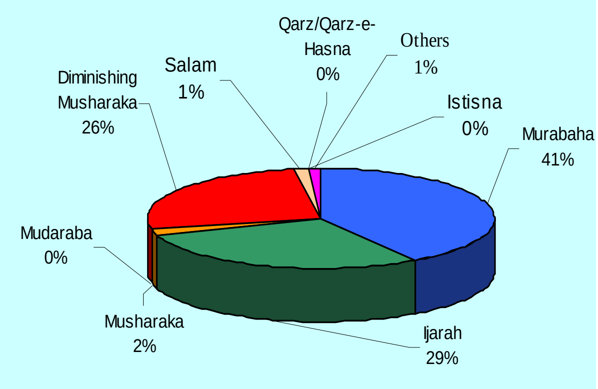
Figure-5.1: Composition of Deposits



during the quarter under review.

The deposits have grown by 14.9 percent in Sep-07. The breakup of deposits reveals that fixed deposits have increased from 36.6 percent in Jun-07 to 38.0 percent in Sep-07, whereas saving deposits have increased from 29.2 percent in Jun-07 percent to 31.0 percent in Sep-07. Current Account non remunerative deposits have declined from 22.0 percent in Jun-07 to 19.7 percent in Sep-07 whereas deposits from financial institutions have declined marginally from 11.3 percent in Jun-07 to 10.3 percent in Sep-07 (see **Figure-5.1**).

Figure-5.2: Modes of Financing



The second largest source of funding for Islamic Banking Institutions (IBIs) was capital, which increased by 3.6 percent during the quarter. CAR of IBIs though declined from 21.8 percent in Jun-07 to 19.4 percent in Sep-07, is still higher than the minimum CAR of 8 percent, and therefore place the IBIs in the comfortable position to support the expansion of their businesses.

The financing remained at around 50 percent of total assets of the IB system. The composition of financing reflects that Murabaha continued to be the major source of financing at 41 percent however its share has significantly declined from 45 percent in Jun-07. Similarly the share of Ijarah has declined from 30 percent in Jun-07 to 29 percent in Sep-07. Both these modes of financing have lost their share to Diminishing Musharika, which increased from 20 percent in Jun-07 to 26 percent in Sep-07. The combined share of these three modes of financing forms around 96 percent share in total financing by IBIs (see **Figure-5.2**).

Improvement in asset quality of IBIs is evident from a decline of non-performing finances (NPFs) to total financing ratio from 1.0 percent to 0.9 percent despite an increase in NPFs from Rs790 million in Jun-07 to Rs846 million in Sep-07. The decline in the ratio of NPFs to total financing was largely the result of increase in provisioning which is currently at 108 percent of NPFs (see **Table 5.3**). Financing to deposits ratio declined marginally from 71 percent in Jun-07 to 70 percent in Sep-07, which was 78.4 percent in CY06. In fact, the financing to deposits ratio has constantly been declining since the formative period of the Islamic Banking system; this depicts the increasing diversification of operation as well as availability of other opportunities for deployment of earning assets.

The improved operations have resulted in increased profitability, which is reflected from the profit after tax of Rs1 billion during Jan-Sept-07, which is higher than CY06 full-year figures of Rs0.9 billion. Likewise net markup and non-markup income are higher than CY06 full-year figures (see **Table-5.4**). However, the incidence of higher operating expense as percentage of gross income (73.3 percent) has resulted in lower net markup income to total asset and non-markup income to total assets at 3 percent and 1.1 percent (annualized) respectively. The ROA has consequently stagnated at 0.9 percent throughout the year (see **Table-5.3**). Induction of 2 new IBs and opening of 45 new

Table-5.3: Key Performance Indicators

Percent

Indicator	CY03	CY04	CY05	CY06	Jun 07	Sept 07
NPFs to total financing	0.7	0.9	1.0	1.3	1.0	0.9
Net NPFs to net financing	-	0.2	0.2	0.4	0.0	(0.1)
Provision to NPFs	100.0	82.3	80.6	72.0	102.1	108
Net Markup Income to total assets	1.7	1.4	2.3	2.4	3.1	3.0
Non Markup Income to total assets	2.2	1.4	1.7	0.9	1.2	1.1
Operating Expense to Gross Income	54.6	65.3	49.9	72.8	72.2	73.3
ROA (average assets)	2.2	1.2	1.7	0.9	0.9	0.9
Growth in Assets	84.5	241.8	62.0	66.9	17.2	11.8
Growth in Deposits	64.6	259.5	65.4	67.7	16.4	14.9
Growth in Financing	147.0	218.2	66.3	43.3	12.6	12.0

Table-5.4: Income Statement

(Rs. Billion)

	CY03	CY04	CY05	CY06	Jun 07	Sept 07
Markup Income	0.4	1.1	3.2	6.4	5.4	8.7
Markup Expense	0.2	0.5	1.5	3.5	2.9	4.7
Net Markup Income	0.2	0.6	1.6	2.9	2.5	4.0
Provision Expense	(0.0)	0.0	0.2	0.2	0.2	0.3
Non Markup Income	0.3	0.6	1.2	1.1	0.9	1.5
Operating Expense	0.3	0.8	1.4	2.9	2.5	4.0
Profit Before Tax	0.2	0.4	1.2	0.8	0.8	1.2
Tax	0.0	0.0	0.3	(0.0)	0.1	0.1
Profit After Tax	0.2	0.3	1.0	0.9	0.6	1.0

branches by the IBIs since 2006, induction of qualified and experienced personnel as well as institution of technology and risk management regime may well explain the increase in operating expenses.

The overall performance of IBIs during the quarter remained promising. With improving asset quality and profitability coupled with capital adequacy above the required ratio and expanding branch network, the IBIs appear to be firmly placed to gain further share in the banking system.

6 Resilience of the Banking System Based on Stress Tests

As part of the ongoing assessment of resilience of the banking system towards plausible shocks, stress tests have been carried out and are briefly discussed in this segment. This exercise assesses the impact of various shock scenarios on the banking system. The methodology used is simple sensitivity analysis and the reference scenarios have been devised using both the historical as well as hypothetical changes in the risk factors. The impact of the shocks has been assessed for both individual banks as well as all the three commercial banking groups viz. Public Sector Commercial Banks (PSCBs), Local Private Banks (LPBs) and Foreign Banks (FBs) (see **Box 6.1**).

Box: 6.1

Reference Scenarios for Stress Tests

For the Year ended on September 30, 2007

Credit Shocks

Scenario C-1 assumes a 10 percent increase in NPLs (with a provisioning rate of 100 percent).

Scenario C-2 assumes a downward shift of NPLs from Substandard to Doubtful and from Doubtful to Loss category.

Scenario C-3 assumes a cumulative impact of the two shocks under Scenarios 1and 2.

Scenario C-4 assumes an increase in NPLs upto 10%age points rise in NPLs to Loans ratio of consumer finance (with 100% provisioning against increased NPLs)

Market Risk: Interest Rate Shocks

Scenario IR-1 assumes an increase in interest rates by 200 basis points.

Scenario IR-2 assumes a shift and steepening in the yield curve by increasing interest rates of all the three maturities (by 50, 100, and 150 basis points)

Scenario IR-3 assumes a shift coupled with flattening of the yield curve by increasing 150,120 and 100 basis points in the three maturities respectively (almost same as was increased from Aug-03 to Dec-03).

Market Risk: Exchange Rate Shocks

Scenario ER-1 assumes a depreciation of ER by 13 percent (closer to the highest change in the monthly average PRS/US$ exchange rate (12.83) over the period since 1994, in September 2000).

Scenario ER-2 is based on the hypothetical assumption of appreciation of rupee by 10 percent.

Market Risk: Equity Price Risk Shocks

Scenario E-1 assumes the impact of a 20 percent decline in the price of stock holding.

Scenario E-2 assumes the impact of a 40 percent decline in the price of stock holdings.

Liquidity Shocks

Scenario L-1 assumes a 5 percent decline in the liquid liabilities and its impact on liquidity coverage ratio calculated after excluding Govt. securities under Held to Maturity category from liquid assets.

Scenario L-2 assumes a 10 percent decline in the liquid liabilities and its impact on liquidity coverage ratio calculated after excluding Govt. securities under Held to Maturity category from liquid assets.

The impact of credit and market shocks has been gauged in terms of change in profits and is calibrated on capital adequacy ratio (CAR) of the banks.

Box : 6.2

"Stress Tests" on Commercial Banks

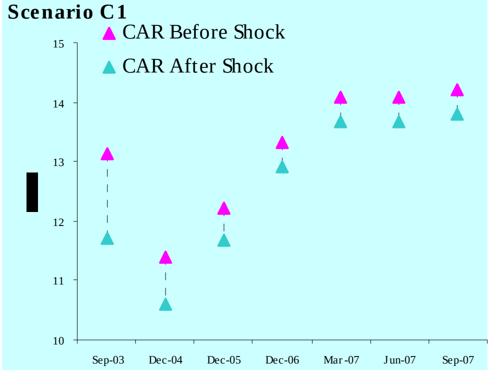
Shocks			September 30, 2007		June 30, 2007	
			%age Point Change in CAR	*Adjusted CAR-After Shock*	*%age Point Change in CAR*	*Adjusted CAR-After Shock*
Credit Shocks						
Scenario	C-1	Deterioration in the qualityof loan	-0.5	13.8	-0.4	13.7
Scenario	C-2	Shift in categories of classified loans	-0.4	13.8	-0.4	13.7
Scenario	C-3	Cumulative impact of all shocks in 1and 2	-0.9	13.3	-0.8	13.3
Scenario	C-4	Deterioration in NPLs ratio of consumer finance	-1.0	13.2	-1.0	13.1
Market Shocks; Interest Rate Shocks						
Scenario	IR-1	Shift in the yield curve	-0.7	13.5	-0.6	13.5
Scenario	IR-2	Shift and steepening of the yield curve	-0.5	13.7	-0.4	13.7
Scenario	IR-3	Shift & flattenining of the yield curve	-0.4	13.9	-0.3	13.8
Market Shocks; Exchange Rate Shocks						
Scenario	ER-1	Depreciation of Rs/US$ exchnage rate (the historical high)	1.1	15.3	1.3	15.4
Scenario	ER-2	Appreciation of Rs/US$ exchnage rate (hypothetical)	-0.9	13.3	-1.0	13.1
Market Shocks; Equity Price Shocks						
Scenario	E-1	Fall in the KSE index (historical high)	-0.1	14.2	0.0	14.1
Scenario	E-2	Fall in the KSE index (hypothetical scenario)	-0.3	13.9	-0.2	13.9
Liquidity Shocks						
Liquidity Coverage Ratio			***Actual***	***Stressed***	***Actual***	***Stressed***
Scenario	L-1	5 Percent Fall in the Liquid Liabilities	40.9	37.8	40.0	36.9
Scenario	L-2	10 Percent Fall in the Liquid Liabilities	40.9	34.3	40.0	33.3

Note: The results have not been adjusted for deferred tax benefits accruing on these losses.

For liquidity shocks, the after shock liquidity coverage ratio[6] is calculated. The summary results of the impact of these shocks are presented in **Box 6.2.**

Fortifying capital base has lent greater resilience to the banking system against the adverse shocks. Under the **Credit Scenario C-1** capital of all banks can fairly absorb this increase in NPLs. Group-wise, none of the groups would experience a fall in its CAR to below 8 percent minimum acceptable level. CAR of PSCBs would experience the largest decline of 0.6 percentage points. Foreign banks with already low level of NPLs would experience a least hit (see **Figure: 6.1**).

Figure:-6.1 Impact of 10% Rise in NPLs on CAR-Scenario C1

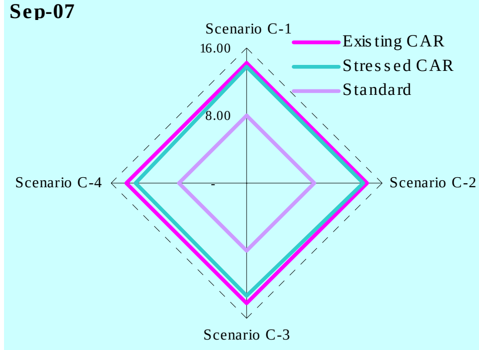


An adverse shift in the categories of NPLs, assumed under **Scenario C-2** would also

[6] Ratio of liquid assets to liquid liabilities

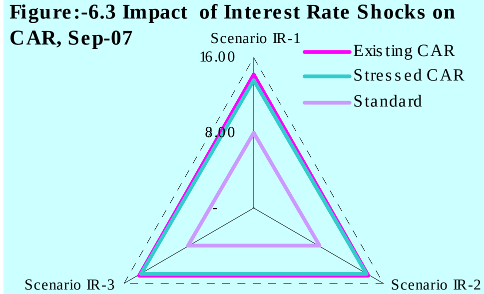
be well absorbed by the banks. In fact, more than 70 percent of NPLs lie in loss category against which a provision of 100 percent is required, therefore, this adverse shift in NPLs would not significantly affect the capital position of the banks. Combined affect of these two scenarios, under **Scenario C-3** would also be absorbed by the banks. In this case, CAR of CBs would decline by less than 1 percentage points under this scenario.

Figure:-6.2 Impact of Credit Shocks on CAR, Sep-07



Considering the pressures on the asset quality of consumer segment the banks resilience has also been assessed towards significant decline in the asset quality of this segment. Under **Credit Scenario C-4,** which takes into account a 10 percent rise in NPLs to loans ratio of consumer finance, the impact remained comparatively higher. Group-wise, FBs followed by LPBs having significant exposure in consumer sector would experience a greater decline in their CAR. The CBs would experience a decline of around 1 percentage point in terms of CAR (see **Figure:-6.2**). Individually, four banks holding a share of around 13 percent in the assets of banking system would experience a decline in their CAR to below 8 percent under this shock.

Figure:-6.3 Impact of Interest Rate Shocks on CAR, Sep-07



Under the market shocks **Scenario IR-1,** the CAR of CBs may experience a decline by 0.7 percentage points (see **Figure: -6.3**). Under **Scenario IR-2**, the impact would be comparatively on lower side. CAR of CBs may decline by 0.5 percentage points to 13.7 percent under this scenario. A flattening in the yield curve assumed under **Scenario IR-3,** would be further reduced and may cause a decline of 0.4 percentage points in CAR of the CBs.

The exchange rate shocks have been assumed under **Scenario ER-1 & ER-2.** The first scenario considers a historical level of depreciation in the rupee by 13 percent. Since foreign currency assets of banks well exceed the foreign exchange liabilities, the banks would rather gain from the depreciation (see **Figure:-6.4**). However, under the second scenario of appreciation of rupee the CAR of CBs may decline by 0.9 percentage points.

Figure:-6.4 Impact of Exchange Rate Shocks on CAR, Sep-07

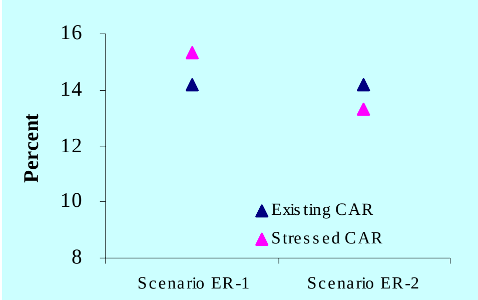
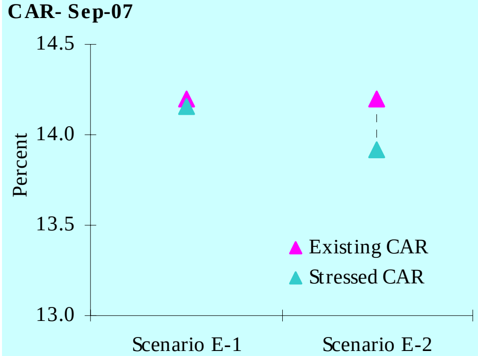


Figure:-6.5 Impact of Equity Price Shocks on CAR- Sep-07

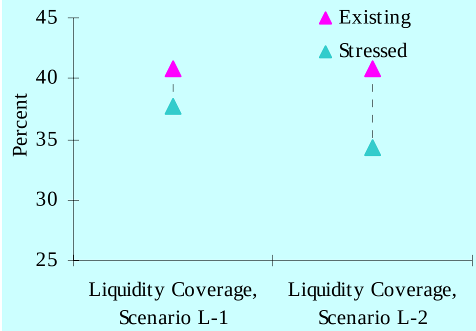


Under **Scenario E-1,** an equity price shock, which assume a 20% fall in the direct equity investment, the banks can sustain this level of shock. Since quite a few banks do not have exposure in equities and the rest of the banks have sufficient surplus available against such share, the impact of this shock is insignificant. Under this shock, CAR of CBs would decline by 0.1 percentage pints (see **Figure:-6.5**). Under **Scenario E-2**, a 40 percent fall in the value of equity investments may decrease the CAR of CBs by 0.3 percentage points. Bank wise, CAR of none of the CBs would fall to below 8 percent under the equity price shocks.

Liquidity coverage ratio has been used to express the level of liquidity of the banks. During the Sep-07 quarter this ratio of the banks has improved significantly. The analysis shows that a 5 percent decline in liquid liabilities, a shock assumed under **Scenario L-1,** the liquidity coverage ratio (calculated after excluding HTM securities from liquid assets) of CBs declined from 40.9 percent to 37.8 percent (see **Figure:-6.6**). Whereas, under a 10 percent decline in the liquid liabilities, **Scenario L-2,** may decrease this ratio to 34.3 percent.

Summing up, the fortified capital base has added to the resilience of the banking system.

Figure:-6.6 Liquidity Coverage Ratio Calculated After Excluding HTM Portfolio-Sep-07



Financial Soundness Indicators of the Banking System

Annex-I

Indicators	2000	2001	2002	2003	2004	2005	2006	Jun-07	Sep-07
CAPITAL ADEQUACY									
Risk Weighted CAR									
Public Sector Commercial Banks	10.4	9.6	12.3	11.0	13.4	14.5	15.2	16.2	17.1
Local Private Banks	9.2	9.5	9.7	9.0	10.1	10.6	12.7	13.2	13.4
Foreign Banks	18.0	18.6	23.2	23.0	17.4	16.4	15.0	14.0	14.9
Commercial Banks	**11.4**	**11.3**	**12.6**	**11.1**	**11.4**	**11.9**	**13.3**	**13.8**	**14.2**
Specialized Banks	(3.3)	(13.9)	(31.7)	(28.2)	(9.0)	(7.7)	(8.3)	(7.3)	(8.0)
All Banks	**9.7**	**8.8**	**8.8**	**8.5**	**10.5**	**11.3**	**12.7**	**13.3**	**13.6**
Tier 1 Capital to RWA									
Public Sector Commercial Banks	7.7	7.1	8.6	8.2	8.6	8.8	11.1	11.9	13.0
Local Private Banks	8.1	8.4	6.6	7.0	7.5	8.3	10.4	10.9	11.3
Foreign Banks	17.9	18.6	23.0	23.0	17.1	16.1	14.3	13.3	14.2
Commercial Banks	**9.8**	**9.7**	**9.7**	**9.1**	**8.6**	**9.1**	**10.8**	**11.2**	**11.8**
Specialized Banks	(3.4)	(13.9)	(31.7)	(28.7)	(15.0)	(13.6)	(13.3)	(12.7)	(13.4)
All Banks	**8.3**	**7.3**	**6.2**	**6.5**	**7.6**	**8.3**	**10.0**	**10.6**	**11.1**
Capital to Total Assets									
Public Sector Commercial Banks	4.6	3.7	5.6	6.1	8.7	12.6	12.2	12.4	13.4
Local Private Banks	3.5	3.8	5.2	5.3	6.5	7.0	9.2	9.8	9.9
Foreign Banks	8.8	8.5	10.6	9.9	8.9	9.5	10.1	9.6	11.2
Commercial Banks	**4.9**	**4.6**	**6.1**	**6.1**	**7.2**	**8.4**	**9.9**	**10.3**	**10.6**
Specialized Banks	(1.1)	(10.3)	(23.0)	(10.0)	(9.4)	(8.1)	(8.0)	(6.2)	(7.5)
All Banks	**4.5**	**3.8**	**4.8**	**5.5**	**6.7**	**7.9**	**9.4**	**9.9**	**10.2**
ASSET QUALITY									
NPLs to Total Loans									
Public Sector Commercial Banks	26.3	25.9	25.5	20.4	13.3	10.0	9.0	8.3	9.1
Local Private Banks	15.4	16.3	15.4	11.3	9.0	6.4	5.2	5.7	6.1
Foreign Banks	4.7	4.3	3.8	3.1	1.6	1.2	1.0	1.1	1.2
Commercial Banks	**19.5**	**19.6**	**17.7**	**13.7**	**9.0**	**6.7**	**5.7**	**6.0**	**6.5**
Specialized Banks	52.4	53.0	54.7	55.6	54.1	46.0	39.1	37.9	38.9
All Banks	**23.5**	**23.4**	**21.8**	**17.0**	**11.6**	**8.3**	**6.9**	**7.1**	**7.7**
Provision to NPLs							0		
Public Sector Commercial Banks	59.2	56.6	57.1	65.8	77.0	86.8	84.5	84.5	79.8
Local Private Banks	36.9	40.5	58.6	62.7	69.9	76.4	78.7	72.7	70.5
Foreign Banks	65.9	74.1	73.3	78.7	101.9	145.9	191.7	188.9	181.6
Commercial Banks	**53.9**	**53.2**	**58.2**	**64.8**	**72.4**	**80.4**	**81.5**	**76.9**	**73.7**
Specialized Banks	58.1	59.2	66.9	61.5	64.9	64.8	64.1	62.9	62.6
All Banks	**55.0**	**54.7**	**60.6**	**63.9**	**70.4**	**76.7**	**77.8**	**74.3**	**71.7**
Net NPLs to Net Loans									
Public Sector Commercial Banks	12.7	13.1	12.8	8.1	3.4	1.5	1.5	1.4	2.0
Local Private Banks	10.3	10.4	7.0	4.5	2.9	1.6	1.1	1.6	1.9
Foreign Banks	1.7	1.1	1.1	0.7	(0.0)	(0.6)	(1.0)	(1.0)	(1.0)
Commercial Banks	**10.1**	**10.3**	**8.3**	**5.3**	**2.7**	**1.4**	**1.1**	**1.4**	**1.8**
Specialized Banks	31.6	31.5	28.5	32.5	29.3	23.1	18.7	18.5	19.2
All Banks	**12.2**	**12.1**	**9.9**	**6.9**	**3.8**	**2.1**	**1.6**	**1.9**	**2.3**
Net NPLs to Capital									
Public Sector Commercial Banks	124.5	160.2	83.4	50.0	16.2	5.5	6.4	5.4	7.2
Local Private Banks	153.5	125.2	54.8	39.1	24.3	13.0	7.1	9.6	9.6
Foreign Banks	9.0	5.8	4.7	3.2	(0.2)	(3.0)	(5.1)	(5.0)	(4.3)
Commercial Banks	**96.7**	**100.7**	**54.2**	**36.9**	**19.0**	**9.0**	**6.2**	**7.8**	**8.5**
Specialized Banks	-	-	-	-	-	-	-	-	-
All Banks	**131.3**	**150.5**	**85.5**	**54.4**	**29.2**	**14.3**	**9.7**	**10.7**	**11.4**
EARNINGS									
Return on Assets (Before Tax)									
Public Sector Commercial Banks	0.5	-	1.3	1.8	2.4	3.3	4.0	3.8	4.1
Local Private Banks	(0.1)	0.9	1.4	2.2	1.7	2.7	3.1	3.0	2.9
Foreign Banks	1.4	1.7	2.3	2.6	2.5	3.6	3.2	2.3	2.0
Commercial Banks	**0.4**	**0.6**	**1.5**	**2.1**	**2.0**	**2.9**	**3.2**	**3.1**	**3.1**
Specialized Banks	(2.3)	(8.4)	(10.2)	(3.3)	(0.4)	(1.0)	(1.3)	0.7	(0.6)
All Banks	**0.3**	**0.1**	**0.9**	**1.8**	**1.9**	**2.8**	**3.1**	**3.0**	**3.0**
Return on Assets (After Tax)									
Public Sector Commercial Banks	0.2	(0.5)	0.6	1.0	1.3	2.2	2.7	2.5	2.9
Local Private Banks	(0.7)	0.4	0.8	1.4	1.2	1.8	2.1	2.0	1.9
Foreign Banks	0.6	0.8	1.5	1.5	2.0	2.5	2.1	1.3	1.0
Commercial Banks	**(0.0)**	**(0.0)**	**0.8**	**1.2**	**1.3**	**2.0**	**2.2**	**2.1**	**2.1**
Specialized Banks	(2.3)	(8.8)	(12.1)	(3.7)	(0.8)	(1.2)	(1.8)	0.6	(0.9)
All Banks	**(0.2)**	**(0.5)**	**0.1**	**1.0**	**1.2**	**1.9**	**2.1**	**2.0**	**2.0**

Indicators	2000	2001	2002	2003	2004	2005	2006	Jun-07	Sep-07
ROE (Avg. Equity & Surplus) (Before Tax)									
Public Sector Commercial Banks	10.9	0.5	26.3	29.9	30.8	30.7	32.4	30.4	32.2
Local Private Banks	(3.2)	25.4	32.3	41.5	28.8	40.1	36.2	31.1	29.5
Foreign Banks	15.6	19.3	24.2	25.0	26.7	38.9	30.0	23.3	18.0
Commercial Banks	**8.8**	**12.2**	**27.5**	**33.7**	**29.0**	**37.2**	**34.7**	**30.5**	**29.7**
Specialized Banks	-	-	-	-	-	-	-	-	-
All Banks	**5.7**	**1.4**	**21.1**	**35.4**	**30.5**	**38.2**	**35.2**	**31.0**	**30.1**
ROE (Avg. Equity & Surplus) (After Tax)									
Public Sector Commercial Banks	4.9	(12.2)	11.5	17.3	17.2	20.9	21.7	20.3	22.6
Local Private Banks	(17.4)	10.3	17.3	25.8	20.2	27.2	25.0	20.7	19.6
Foreign Banks	6.1	9.1	15.2	14.8	21.5	27.1	20.4	13.2	8.8
Commercial Banks	**(0.3)**	**(0.3)**	**14.3**	**20.3**	**19.6**	**25.4**	**23.7**	**20.2**	**19.9**
Specialized Banks	-	-	-	-	-	-	-	-	-
All Banks	**(3.5)**	**(12.6)**	**3.2**	**20.0**	**20.3**	**25.8**	**23.8**	**20.6**	**20.0**
NII/Gross Income							-		
Public Sector Commercial Banks	61.8	69.9	69.5	64.1	63.7	71.3	69.5	75.9	68.7
Local Private Banks	63.2	72.1	65.5	55.9	62.0	73.0	73.5	72.8	71.7
Foreign Banks	54.0	59.4	57.5	55.3	57.7	61.5	65.8	61.2	57.7
Commercial Banks	**61.2**	**68.9**	**66.1**	**58.9**	**61.9**	**71.3**	**72.1**	**72.6**	**70.5**
Specialized Banks	78.6	86.7	78.0	62.2	81.9	87.7	40.1	52.2	57.9
All Banks	**62.3**	**70.4**	**67.1**	**59.2**	**62.8**	**72.0**	**70.9**	**71.7**	**70.0**
Cost / Income Ratio									
Public Sector Commercial Banks	70.1	62.3	56.9	43.9	39.5	34.3	31.8	33.1	31.0
Local Private Banks	80.9	67.3	60.0	53.2	56.2	43.1	40.7	43.4	44.5
Foreign Banks	59.4	54.5	45.4	48.2	49.0	42.2	49.8	52.9	54.7
Commercial Banks	**71.6**	**62.7**	**56.7**	**49.0**	**51.7**	**41.2**	**39.4**	**42.1**	**42.3**
Specialized Banks	70.5	59.0	84.7	67.5	57.8	47.8	62.6	49.2	41.8
All Banks	**71.6**	**62.4**	**59.1**	**50.5**	**52.0**	**41.5**	**40.3**	**42.4**	**42.3**
LIQUIDITY									
Liquid Assets/Total Assets									
Public Sector Commercial Banks	37.1	36.5	49.0	49.1	43.9	35.6	33.9	35.8	35.0
Local Private Banks	34.0	39.8	47.1	42.9	34.3	32.4	31.1	35.6	36.5
Foreign Banks	45.2	50.3	48.5	49.2	39.8	41.8	41.0	42.0	43.1
Commercial Banks	**37.5**	**39.9**	**48.1**	**46.1**	**37.0**	**33.9**	**32.2**	**36.0**	**36.5**
Specialized Banks	12.7	13.6	16.4	22.9	25.3	25.8	23.0	26.4	19.4
All Banks	**36.0**	**38.5**	**46.7**	**45.1**	**36.6**	**33.7**	**31.9**	**35.8**	**36.1**
Liquid Assets/Total Deposits									
Public Sector Commercial Banks	45.0	43.4	59.6	59.0	52.6	44.7	42.6	45.7	43.9
Local Private Banks	44.3	49.6	60.2	54.5	42.3	40.3	40.6	46.8	47.6
Foreign Banks	67.7	78.3	74.2	68.9	53.4	57.9	61.1	63.1	59.9
Commercial Banks	**48.0**	**50.3**	**61.5**	**57.8**	**45.7**	**42.7**	**42.0**	**47.4**	**47.3**
Specialized Banks	90.8	79.8	98.5	135.0	154.1	183.2	205.4	238.5	183.2
All Banks	**48.5**	**50.7**	**61.8**	**58.5**	**46.5**	**43.5**	**42.7**	**48.1**	**47.7**
Advances/Deposits									
Public Sector Commercial Banks	54.0	53.8	44.3	45.7	49.7	59.8	64.6	61.5	61.0
Local Private Banks	67.5	57.9	52.3	58.2	67.3	70.8	74.5	67.0	65.8
Foreign Banks	71.5	66.8	72.0	63.8	70.1	68.7	80.1	73.6	68.2
Commercial Banks	**60.5**	**56.9**	**51.0**	**53.6**	**63.6**	**68.4**	**72.7**	**66.1**	**64.9**
Specialized Banks	553.0	450.5	453.8	379.1	370.5	400.7	528.4	525.4	587.9
All Banks	**66.2**	**61.7**	**54.9**	**56.4**	**65.8**	**70.2**	**74.6**	**67.8**	**66.6**

Note: The indicators for June & September 2007 are based on Un-audited returns.

Selected Indicators for Different Categories of Banks, September 30, 2007- Annex-II

Indicators	Top 5 Banks	Top 10 Banks	Top 20 Banks	Industry
Share of Total Assets	50.6%	73.4%	93.3%	100%
Share of Total Deposits	53.1%	76.7%	94.4%	100%
Share of Gross Income	56.0%	77.4%	96.0%	100%
Share of Risk Weighted Assets	49.8%	71.9%	92.5%	100%
Capital Adequacy				
Capital/RWA	14.9%	14.0%	13.6%	13.6%
Tier 1 Capital / RWA	11.9%	11.4%	11.0%	11.1%
Net Worth / Total Assets	10.3%	10.2%	10.1%	10.2%
Asset Composition				
Sectoral Distribution of Loans (Domestic)				
- Corporate Sector	46.3%	73.9%	93.7%	100%
- SMEs	48.5%	68.4%	90.4%	100%
- Agriculture	37.5%	46.2%	95.9%	100%
- Consumer Finance	55.4%	75.9%	97.8%	100%
- Commodity Financing	57.6%	78.4%	81.7%	100%
- Staff Loans	63.7%	81.8%	96.4%	100%
- Others	19.6%	45.3%	59.9%	100%
- **Total**	**48.2%**	**71.8%**	**92.6%**	**100%**
NPLs / Gross Loans	8.0%	7.1%	7.2%	7.7%
Net NPLs / Capital	10.6%	9.2%	11.2%	11.4%
Earning & Profitability				
ROA	2.5%	2.4%	2.1%	2.0%
ROE	25.3%	23.8%	21.4%	20.1%
Net Interest Income / Gross Income	74.4%	72.4%	70.9%	70.0%
Income from Trading & Foreign Exchange / Gross Income	14.7%	16.1%	16.3%	16.4%
Non-Interest Expense / Gross Income	36.3%	37.9%	40.4%	42.3%
Liquidity				
Liquid Assets / Total Assets	37.3%	36.1%	35.9%	36.0%
Liquid Assets held in Govt. Securities / Total Liquid Assets	60.9%	61.2%	58.5%	57.0%
Liquid Assets / Total Deposits	47.1%	45.7%	46.9%	47.6%

Major Banking Statistics, September 30, 2007 **Annex-III**

(Rs in Millions)

S.No.	Name of Bank	Assets	Deposits	Equity
1	The Bank of Khyber	34,493	23,100	6,256
2	The Bank of Punjab	223,042	191,419	20,858
3	First Women Bank Limited	8,149	6,756	1,046
4	National Bank of Pakistan	667,924	522,929	96,585
5	Industrial Development Bank of Pakistan	8,124	5,841	(27,972)
6	Zarai Taraqiati Bank Limited	86,683	2,613	13,841
7	The Punjab Provincial Cooperative Bank Limited	13,144	1,817	2,796
8	SME Bank Ltd.	6,905	1,878	2,765
9	Allied Bank Limited	280,087	233,835	20,047
10	Bank Alfalah Limited	312,460	260,228	15,362
11	Bank Al-Habib Limited	133,661	109,339	7,726
12	Askari Bank Limited	178,498	142,436	13,285
13	Crescent Commercial Bank Limited	19,026	11,108	6,975
14	Atlas Bank Limited	21,937	12,630	2,967
15	Habib Bank Ltd	622,742	506,564	58,738
16	Faysal Bank Limited	144,278	105,902	16,966
17	KASB Bank Ltd	37,521	30,616	2,866
18	Dubai Islamic Bank Pakistan Limited	17,069	12,422	3,930
19	JS Bank Limited	20,757	11,689	3,411
20	Bank Islami Pakistan Limited	9,985	6,246	3,169
21	Arif Habib Rupali Bank Limited	13,788	7,363	6,181
22	Emirates Global Islamic Bank Limited	7,485	4,271	2,831
23	First Dawood Islamic Bank Limited	4,434	1,071	3,038
24	ABN Amro Bank N.V.	116,045	95,743	6,760
25	MCB Bank Limited	382,594	287,922	48,129
26	Meezan Bank Limited	64,236	51,657	5,436
27	Habib Metropolitan Bank Limited	173,053	132,030	12,780
28	Mybank Limited	37,229	27,983	5,682
29	NIB Bank Limited	109,686	45,308	22,565
30	PICIC Commercial Bank Limited	82,471	62,246	4,734
31	Saudi Pak Commercial Bank Limited	60,759	43,465	5,194
32	Soneri Bank Limited	74,016	57,976	6,419
33	United Bank Limited	483,398	380,752	34,785
34	Standard Chartered Bank (Pakistan) Limited	259,238	172,594	44,143
35	Oman International Bank	2,674	591	2,028
36	The Hong Kong and Shanghai Banking Corp. Ltd.	29,106	21,784	2,560
37	Deutche Bank AG	11,956	3,791	3,170
38	The Bank of Tokyo-Mitsubishi-UFJ, Limited	4,854	1,410	2,326
39	Citibank N.A.	101,672	80,252	6,537
40	Albarka Islamic Bank	18,528	13,744	2,365
		4,883,705	**3,691,321**	**499,280**

Annex-IV

Group-wise Composition of Banks

1997-1998	2005	2006	Sep-07
A. Public Sector Com. Banks (6)	**A. Public Sector Com. Banks (4)**	**A. Public Sector Com. Banks (4)**	**A. Public Sector Com. Banks (4)**
Habib Bank Ltd.	National Bank of Pakistan	National Bank of Pakistan	National Bank of Pakistan
National Bank of Pakistan	First Women Bank Ltd.	First Women Bank Ltd.	First Women Bank Ltd.
United Bank Ltd.	The Bank of Khyber	The Bank of Khyber	The Bank of Khyber
First Women Bank Ltd.	The Bank of Punjab	The Bank of Punjab	The Bank of Punjab
The Bank of Khyber	**B. Local Private Banks (20)**	**B. Local Private Banks (24)**	**B. Local Private Banks (26)**
The Bank of Punjab	Askari Commercial Bank Ltd.	Askari Commercial Bank Ltd.	Askari Bank Ltd.
B. Local Private Banks (16)	Bank Al-Falah Ltd.	Bank Alfalah Ltd.	Bank Alfalah Ltd.
Askari Commercial Bank Ltd.	Bank Al Habib Ltd.	Bank AL Habib Ltd.	Bank AL Habib Ltd.
Bank Alfalah Ltd.	My Bank Ltd.	Mybank Limited	Mybank Limited
Bank AL Habib Ltd.	Faysal Bank Ltd.	Faysal Bank Ltd.	Faysal Bank Ltd.
Bolan Bank Ltd.	Metropolitan Bank Ltd.	Habib Metropolitan Bank Ltd.	Habib Metropolitan Bank Ltd.
Faysal Bank Ltd.	KASB Bank Ltd.	KASB Bank Ltd.	KASB Bank Ltd.
Metropolitan Bank Ltd.	Prime Commercial Bank Ltd.	Prime Commercial Bank Ltd.	ABN AMRO Bank (Pakistan) Ltd 1
Platinum Commercial Bank Ltd.	Saudi Pak Commercial Bank Ltd	Saudi Pak Commercial Bank Ltd	Saudi Pak Commercial Bank Ltd
Prime Commercial Bank Ltd.	PICIC Commercial Bank Ltd.	PICIC Commercial Bank Ltd.	PICIC Commercial Bank Ltd.
Prudential Commercial Bank Ltd	Soneri Bank Ltd.	Soneri Bank Ltd.	Soneri Bank Ltd.
Gulf Commercial Bank Ltd.	Union Bank Ltd.	Standard Chartered Bank (Pakistan) Ltd.	Standard Chartered Bank (Pakistan) Ltd.
Soneri Bank Ltd.	MCB Bank Ltd.	MCB Bank Ltd.	MCB Bank Ltd.
Union Bank Ltd.	Allied Bank Limited.	Allied Bank Limited	Allied Bank Limited
Muslim Commercial Bank Ltd.	United Bank Ltd.	United Bank Ltd.	United Bank Ltd.
Allied Bank of Pakistan	Meezan Bank Limited	Meezan Bank Limited	Meezan Bank Limited
Trust Bank Ltd.	NIB Bank Ltd.	NIB Bank Limited	NIB Bank Limited
Indus Bank Ltd.	Crescent Commercial Bank Ltd.	Crescent Commercial Bank Ltd.	Crescent Commercial Bank Ltd.
C. Foreign Banks (20)	Habib Bank Ltd	Habib Bank Limited	Habib Bank Limited
ABN AMRO Bank N.V.	Dawood Bank Ltd.	Atlas Bank Limited.	Atlas Bank Limited.
Albaraka Islamic Bank B.S.C.	**C. Foreign Banks (11)**	Arif Habib Rupali Bank Ltd.	Arif Habib Bank Ltd.
American Express Bank Ltd.	ABN AMRO Bank N.V.	Dubai Islamic Bank Pakistan Ltd.	Dubai Islamic Bank Pakistan Ltd.
ANZ Grindlays Bank	Albaraka Islamic Bank B.S.C.	BankIslami Pakistan Ltd.	BankIslami Pakistan Ltd.
Bank of America	American Express Bank Ltd [7].	JS Bank Limited	JS Bank Limited
Bank of Ceylon	The Bank of Tokyo – Mitsubishi.	**C. Foreign Banks (7)**	Emirates Global Islamic Bank Ltd.
The Bank of Tokyo - Mitsubishi	Citibank N.A.	ABN AMRO Bank N.V.	Dawood Islamic Bank Ltd
Citibank, N.A.	Deutsche Bank AG	Albaraka Islamic Bank B.S.C.	
Credit Agricole Indosuez	Habib Bank AG Zurich	Bank of Tokyo - Mitsubishi UFJ, Limited	**C. Foreign Banks (6)**
Deutsche Bank AG	The Hongkong & Shanghai Banking Corporation Ltd.	Citibank N.A.	Albaraka Islamic Bank B.S.C.
Doha Bank	Oman International Bank S.A.O.G.	Deutsche Bank AG	Bank of Tokyo - Mitsubishi UFJ, Limited
Emirates Bank International	Rupali Bank Ltd.	The Hongkong & Shanghai Banking Corporation Limited	The Hongkong & Shanghai Banking Corporation Limited
Habib Bank AG Zurich	Standard Chartered Bank	Oman International Bank S.A.O.G.	Deutsche Bank AG
The Hongkong & Shanghai Banking Corporation Ltd	**D. Specialized Banks (4)**		Citibank N.A.
IFIC Bank Ltd.	Zarai Taraqiati Bank Ltd.	**D. Specialized Banks (4)**	Oman International Bank S.A.O.G.
Mashreq Bank PJSC	Industrial Development Bank of Pakistan	Zarai Taraqiati Bank Ltd.	
Oman International Bank S.A.O.G.	Punjab Provincial Co-operative Bank Ltd.	Industrial Development Bank of Pakistan	
Rupali Bank Ltd.	SME Bank Ltd	Punjab Provincial Co-operative Bank Ltd.	**D. Specialized Banks (4)**
Societe Generale	**Commercial Banks (35)**	SME Bank Limited	Zarai Taraqiati Bank Ltd.
Standard Chartered Bank	Include A + B + C	**All Commercial Banks (35)**	Industrial Development Bank of Pakistan
D. Specialized Banks (4)	**All Banks (39)**	Include A + B + C	Punjab Provincial Co-operative Bank Ltd.
Agriculture Development Bank of Pakistan	Include A + B + C + D	**All Banks (39)**	SME Bank Limited
Industrial Development Bank of Pakistan		Include A + B + C + D	**All Commercial Banks (36)**
Federal Bank for Co-operatives			Include A + B + C
Punjab Provincial Co-operative Bank Ltd.			**All Banks (40)**
All Commercial Banks (42)			Include A + B + C + D
Include A + B + C			
All Banks (46)			
Include A + B + C + D			

1. ABN AMRO Bank NV. (Pakistan) branches were descheduled on account of its merger with Prime Commercial Bank. The name of Prime Commercial Bank has been changed to ABN AMRO Bank (Pakistan) Ltd.