

Management Discussion and Analysis



Mohammad Aftab Manzoor
Chief Executive Officer

Profit

The Bank made significant strides towards strategic priorities. Strong growth in key areas enabled us to increase our operating profit by 17% to Rs.8.8 billion. Strong corporate banking performance, increased emphasis on middle market, targeted deposit mobilization, improved customer confidence, largest ATM

network with the widest geographical coverage and strong branch network were few key factors behind the impressive growth.

The after tax profit during FY07, however, slipped by 7% to Rs. 4.1 billion compared to Rs. 4.4 billion for FY06 primarily due to the stricter provisioning rules introduced by the State Bank of Pakistan (SBP) later this

year. The rules disallowed banks to take into account the Forced Sale Value (FSV) of illiquid assets while calculating the provisioning against Non-Performing Loans (NPLs). The Bank has recorded a sum of Rs.1.91 billion under the rules. Eliminating the impact of FSVs, the profit after tax would have increased by 21%.

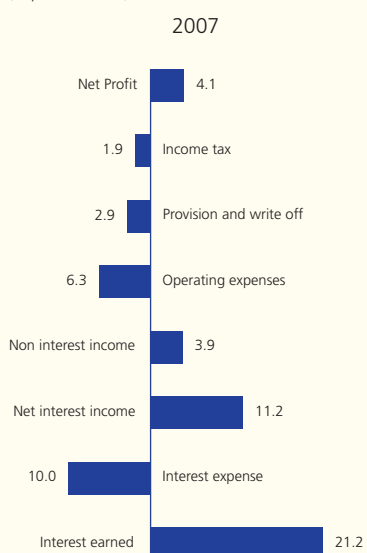
Consequently, Return on Equity (RoE) was down to 23.5% from last year's 30.2%, with Return on Assets (RoA) reaching 1.42% over last year's 1.98%. Without provisioning impact in terms of the rules, RoE and RoA would increase to 30.7% and 1.9% respectively.

The Bank's RoE was rated as one of the top 40 in the world, besides other ratings, by UK's 'The Banker', published by Financial Times London. The categories and ranking are as follows.

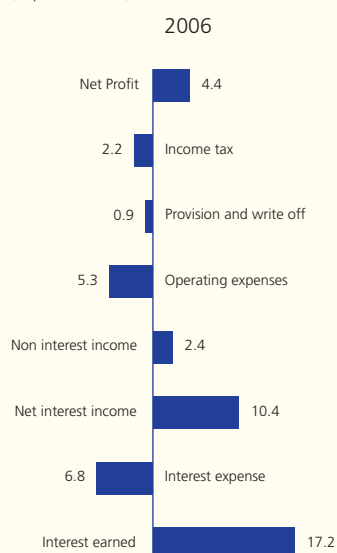
Rank Categories	Rank in the world
Performance based	
Profit on average capital (RoE)	38th
Return on assets (RoA)	131st
Real profit growth	262nd

Soundness based	
Capital assets ratio	523rd
Size based	
Assets	833rd
Overall world ranking	932nd

Profit and Loss Composition
(Rupees in billion)



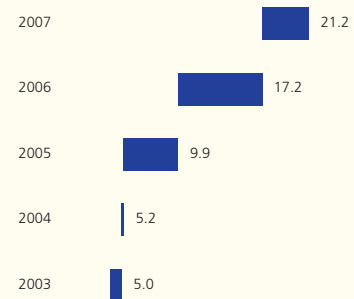
Profit and Loss Composition
(Rupees in billion)



Net Mark-up / Interest Income

Mark-up / interest income of the Bank grew by over 23% to reach Rs.21.2 billion. The quality of growth was given priority over just growing balance sheet. Yet, the Bank was able to grow its average earning assets by 18% with

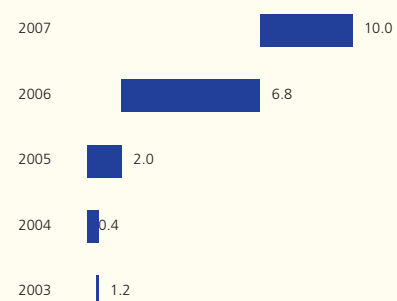
Interest Income
(Rupees in billion)



overall yield improving by over 40 basis points.

Mark-up / interest expense rose to Rs.10.0 billion depicting a rise of 48%, which is remarkably well below 67% annualized growth registered in June 2007 and 236% witnessed in FY06. The growth was driven by a higher contribution from deposits, through a combination of good balance sheet growth and a stable liability margin. Due to the tough competition in banking industry on low cost deposits mobilization front, cost of deposits rose by 60 basis points. The Bank, however, is following a balanced growth trajectory with due weightage given to low cost core deposits yet maintaining stable balance sheet growth.

Interest Expense
(Rupees in billion)

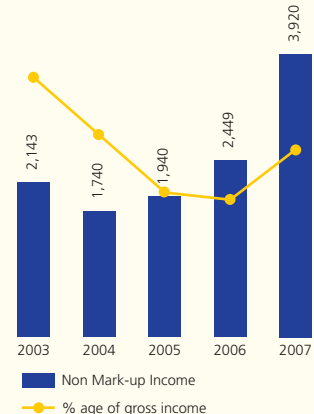


Net mark-up / interest income rose by over 7% to Rs.11.2 billion compared to Rs.10.4 billion. This growth underscores performance due to funds channeled to tax efficient mutual funds, the income whereof appears under non-interest income and is reflected in operating income growth. Despite this, interest rate spread was maintained above 5.0% when compared with past two years' spreads.

Non Mark-up Income

Non mark-up income witnessed an exceptional growth of 60% to Rs.3.9 billion in FY07, contributing over 23% to total operating income, 5.5% up from FY06. Fee, commission and brokerage income grew by over 52% to Rs.2.1 billion. Besides, investment banking income rose to Rs.241 million portraying a growth of 43%, improved income was also driven by increased trade volume and local remittances business.

Non Markup / Interest Income
(Rupees in million)



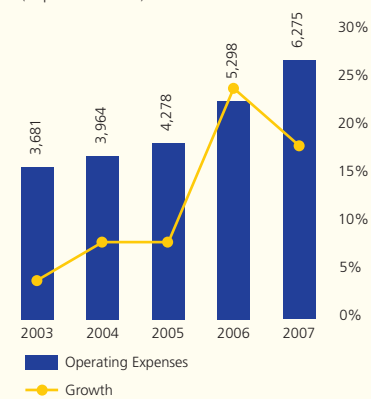
Account maintenance charges grew by over 100% to Rs.408 million. Changing depositors' behavior owing to interalia inflationary pressures, certain changes in our schedule of charges and increased deposit accounts drove this growth during 2007.

Capital gain and dividend income increased significantly by 194% to Rs.1.6 billion compared to Rs.0.5 billion during FY06. This growth was driven primarily by funds directed towards tax efficient mutual funds, which remained one of top yielding earning asset of the Bank. The Bank also continued to capitalize on the opportunities created by buoyant equity market.

Operating Expenses

Owing to our planned expansion coupled with inflationary impact, operating expenses increased by 18% to Rs. 6.3 billion. The 17% rise in operating profit was managed with a modest increase of 9% in human resources cost, reflecting strong cost control measures.

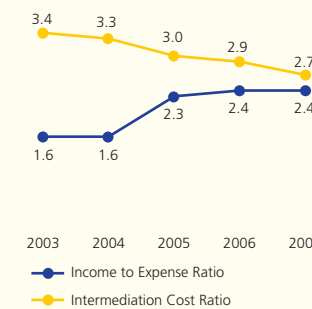
Operating Expenses
(Rupees in million)



The surge in real estate prices proportionately impacted rentals during FY07 and we were not an exception where such expenses increased by over 20%. Our branch renovation plan also contributed to increase in operating expenses as repairs, maintenance and depreciation expense grew by 36% and 43% respectively. These expenses are expected to improve our image and, in turn, would contribute towards Bank's medium to long term growth and profitability.

Cost to revenue ratio maintained its last year's level as it was recorded at 41.4% slightly down from last year's 41.1%. However, Intermediation cost ratio improved to 2.7% compared to 2.9% during FY06.

Intermediation Cost Ratio and Income to Expense Ratio
(Percentage)



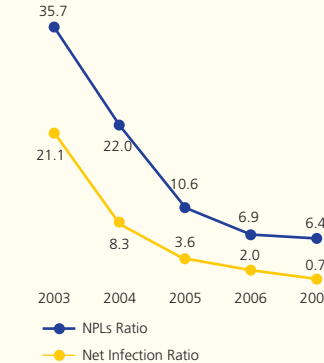
Loans Quality Analysis

In determining the classification of loan portfolio, we align our judgment with a series of criterias that are derived from SBP guidelines. The table below sets forth, as of the dates indicated, the distribution of our loan portfolio by five-category loan classification.

Recent economic slow-down, concerning key economic indicators, law and order situation, global financial and economic events and blurred post-election scenario of our country entails challenges ahead for the banking industry on risk management front.

Rupees in million	December 31, 2007		December 31, 2006	
Performing Loans	167,169	93.6%	141,227	93.1%
Non-Performing Loans				
Other Assets Especially Mentioned	33	0.02%	36	0.02%
Substandard	1,312	0.7%	535	0.4%
Doubtful	533	0.3%	659	0.4%
Loss	9,477	5.3%	9,249	6.1%
Sub-total	11,355	6.4%	10,479	6.9%
Total Advances	178,524		151,705	

NPL Ratios
(Percentage)



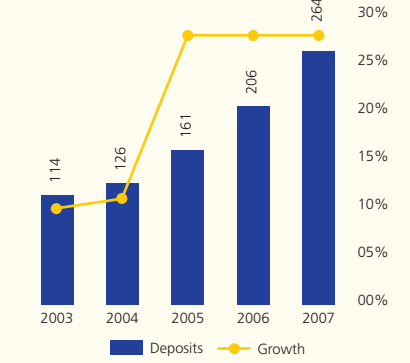
Our Bank is not an exception to this, as Non-Performing Loans (NPLs) saw a slight increase by over 8% to Rs.11.4 billion compared to Rs.10.5 billion last year.

The management is watchful of its loan portfolio and has been pursuing stringent risk management policies with a balanced growth approach. Despite rise in NPLs, NPL ratio improved from last year's 6.9% to 6.4% this year with net infection ratio improved remarkably to 0.74% from 1.96% witnessed last year. The loan loss coverage ratio improved to 89.0% from last year's 73.1%.

Deposits

Customer deposits remained our major source of funding during FY07. Strong M2 growth over the years, improved

Deposits
(Rupees in billion)



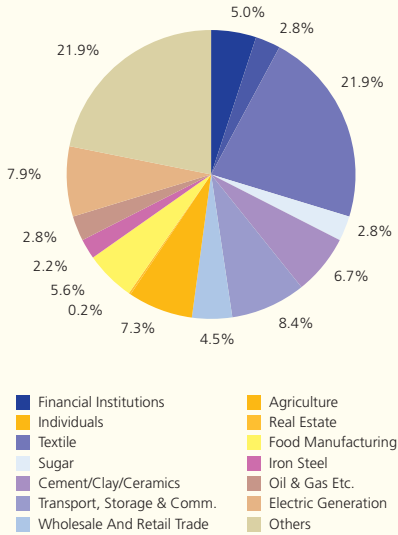
per capita income, increased offered profit rates on deposits, improved customer service, online banking and wide geographical presence helped us to achieve an impressive growth of over 28%. Customer deposits reached Rs.264 billion compared to last year's Rs.206 billion. The deposits thus far have grown at CAGR of 21% over last five years.

Despite tough market conditions, the Bank was not only able to maintain its Current & Saving Accounts (CASA) but also grew these by 13%. New schemes attracted favorable customer response as fixed and other remunerative deposits rose by over 51%, reflecting greater reliance on banking with the Bank. Increased banking by diversified depositor base would also allow us to cross-sell other products going forward.

This impressive growth has enabled us to increase our market share by 50 basis points, in only one year's time, to reach 7.4% by the year end (based on SBP's provisional data).

Management Discussion and Analysis

Advances Segemental Analysis
(Percentage)



The growth was well diversified among various segments and was achieved despite increased dependence of corporate sector on debt instruments.

The management is also watchful of impact of this growth on capital adequacy.

On market share front, the Bank has managed to increase its market share by 40 basis points to 6.7% by the year end (based on SBP's provisional data).

While monitoring the margin available in Capital Adequacy Ratio (CAR), the Bank increased its portfolio wisely among different asset categories and remained vigilant about their impact on CAR as well. Due to this fact coupled with the impact of additional provisioning in terms of the SBP rules, CAR was down to 9.29% as at December 31, 2007 compared to 12.80% as at December 31, 2006.

Earnings Per Share (EPS)

The Earnings per Share of the Bank for the year ended 2007 is Rs. 7.57 per share, down by 7.2% from last year's Rs. 8.16 per share.

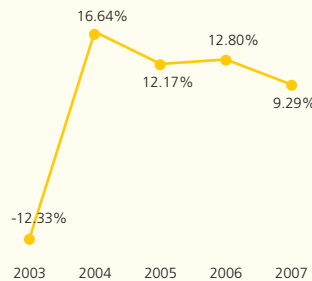
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Loan Book

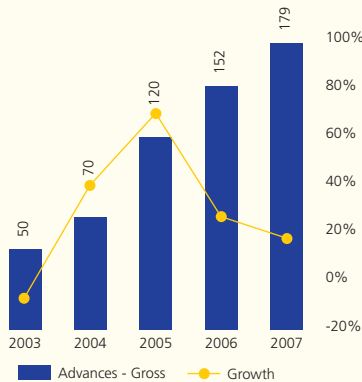
Loan portfolio (gross) of the Bank grew by 18% to Rs.179 billion compared to Rs.152 billion last year with corporate loans and SME loans contributing 80% and 15% respectively of the loan book. With consumer financing on cards for FY08, loan portfolio is expected to further diversify among different products.

Capital Adequacy

Capital Adequacy Ratio
(Percentage)



Advances - Gross
(Rupees in billion)



Risk Weighted Asstes and Regulatory Capital
(Rupees in billion)

