Directors' Report to the Members

On behalf of the Board of Directors (the Board) of MCB Islamic Bank Limited, we are pleased to present the Annual Report for the year ended December 31, 2024.

Rs. in Million

Statement of Financial Position	31-Dec-24	31-Dec-23	Growth
Deposits	209,109	204,460	2.3%
Total Assets	307,344	267,000	15%
Investments – *net*	146,596	132,544	11%
Islamic Financing – *net*	119,353	89,347	34%
Shareholders' Equity *(including revaluations)*	25,946	22,036	18%

Profit & Loss Account	Jan – Dec 2024	Jan – Dec 2023	Growth
Operating income	19,911	18,921	5%
Operating and other expenses	10,259	7,649	34%
Credit loss allowance and write offs – net	(543)	(704)	-77%
Profit before taxation	9,109	10,568	-14%
Profit after taxation	4,239	5,153	-18%
Basic / diluted earnings per share - *Rs.*	2.726	3.314	-18%

Performance Review

Pakistan's banking sector has demonstrated remarkable resilience and strong performance despite the challenges posed by climate change costs, economic stagnation and political instability.

In this dynamic environment, our Bank has strategically focused on sustained growth, Network & business volume expansion and technology investments. Through optimizing deposit mobilization, making timely investments and adhering to prudent financing practices, we have effectively navigated the economic landscape. Supported by an efficient organizational structure, robust risk management and strict regulatory compliance, the Bank achieved a commendable **profit before tax of Rs. 9.11 billion for the year ending December 31, 2024, Alhamdulillah**.

As of December 31, 2024, the Bank's **deposits grew to Rs. 209.11 billion**, up from Rs. 204.46 billion in 2023. The Current and Savings Account (CASA) mix remains healthy at 79%, with non-remunerative deposits comprising 31% of the total. Our commitment to Islamic banking remains strong, as we engage untapped non-banked customers with a diverse range of Islamic banking products, maintaining service excellence.

Total assets surged by 15%, reaching Rs. 307.34 billion by year-end, compared to Rs. 267 billion in 2023. The net financing position rose to Rs. 119.35 billion, up from Rs. 89.35 billion, reflecting prudent financial management, while investments totaled Rs. 146.60 billion. The Bank's capital adequacy ratio increased by 3.30 percentage points, closing at 20.49%. Our management remains focused on efficient capital management, superior asset quality and a high-yielding portfolio.

The Bank generated **operating income of Rs. 19.91 billion**, a 5% increase from the previous year, achieving a return on earning assets of 17.52% and a net spread of 6.80%. However, operating and other expenses increased by 34% due to higher business volumes, substantial branch network expansion and significant investments in infrastructure. This increase is carefully monitored through effective management controls to ensure sustainable profitability.

The Bank reported a **profit after tax of Rs. 4.24 billion**, a slight decrease from Rs. 5.15 billion in the previous year. Earnings per share (EPS) after tax decreased to Rs. 2.73 from Rs. 3.31 in 2023.

A significant milestone during the year was the **Bank's acquisition of 39 branches** from MCB Bank Limited as part of a "Scheme of Compromises, Arrangements and Reconstruction" approved by the Honorable Lahore High Court. Following the Court Order, the banking business, including assets, liabilities and operations of these branches, was converted into Islamic banking branches and transferred to our Bank effective November 15, 2024.

Credit Rating

Pakistan Credit Rating Agency (PACRA) has upgraded the Bank's medium to long-term rating to 'A+' from 'A' and maintained the short-term rating as 'A-1,' with stable outlook.

Economic Review

The global economic landscape has shown modest improvement since June, with stable growth despite persistent challenges. Key structural risks such as high debt burdens, policy uncertainties, climate-related threats, geopolitical tensions, particularly in the Middle East and global trade disruptions continue to pose concerns. Inflationary pressures are easing without triggering a significant slowdown in major economies, leading to a broad shift towards monetary policy easing. The International Monetary Fund (IMF) projects a decline in global inflation from 6.7% in 2023 to 5.7% in 2024. However, economic growth remains insufficient to fully offset the prolonged impact of successive global shocks, particularly in vulnerable economies. Despite these headwinds, the global banking sector remains stable, benefiting from improved financial conditions. The IMF and World Bank forecast global GDP growth of 3.2% [2023: 3.3%] and 2.7% [2023: 2.7%], respectively, for 2024, reflecting a pattern of steady but modest expansion.

Shifting focus to the domestic economy, Pakistan has witnessed positive momentum in the first half of Fiscal Year (FY) 2025, marked by a stable exchange rate, declining inflation and positive real interest rates. The approval of a USD 7 billion Extended Fund Facility (EFF) by the IMF and the announcement of a 10-year Country Partnership Framework (CPF) by the World Bank Group on January 14, 2025, underscore international confidence in Pakistan's economic direction. Investor sentiment remains strong, as reflected in an 84% surge in the Pakistan Stock Exchange since December 2023. Further strengthening the economic stability are rising foreign exchange reserves, a surplus current account and increased private sector credit uptake. The IMF forecasts a GDP growth rate of 2.5% for FY 2024, a notable recovery from the negative 0.2% growth recorded in 2023.

In December 2024, the National Consumer Price Index (CPI) recorded a substantial decline, dropping to 4.1% year-on-year, compared to 29.7% in December 2023. This sharp reduction was primarily driven by lower food prices and favourable global oil trends. The State Bank of Pakistan (SBP) projects headline inflation for FY 2025 to average between 5.5% and 7.5%, indicating a more stable inflationary outlook. In response, from June 2024 to January 2025, the SBP undertook significant monetary easing, reducing the policy rate by 1,000 basis points, bringing it down to 12%, signalling a shift towards a more accommodative monetary stance.

In October 2024, Large-Scale Manufacturing (LSM) recorded a marginal year-on-year growth of 0.02%, marking a shift from the significant contraction of 5.79% observed in October 2023. The current account balance turned surplus at USD 1.21 billion during July–December FY 2025, compared to a deficit of USD 1.4 billion in the same period of the previous year. Exports increased by 7.2% to USD 16.23 billion, while imports rose by 9.3%, widening the trade deficit to USD 11.51 billion. Workers' remittances surged by 32.8%, reaching USD 17.8 billion, further supporting external account stability. As of December 31, 2024, foreign exchange reserves stood at USD 15.93 billion. Reflecting improved investor confidence, the KSE-100 Index closed at 115,127 points, marking an increase of 52,676 points since December 2023.

The Islamic banking industry demonstrated substantial growth in the first half of 2024, with total assets increasing by Rs. 695 billion and deposits rising by Rs. 614 billion. As a result, total assets reached Rs. 9,689 billion, capturing an 18.8% market share, reflecting a 7.7% growth during the period. Deposits totalled Rs. 7,363 billion, representing a 22.7% market share and 9.1% growth. Additionally, the branch network expanded to 5,196 branches by the end of June 2024, further strengthening the industry's outreach and financial inclusion.

Risk Management

The Bank's Risk Management Framework encompasses governance, organizational structure, policies, procedures, risk assessment methodologies, early warning systems and reporting mechanisms. Aligned with the Board's strategy, the independent Risk Management function adheres to international best practices and SBP's guidelines, ensuring comprehensive measurement, analysis and control and monitoring of all risks.

The Risk Management & Portfolio Review Committee, a subcommittee of the Board and Management Finance Committee, provides guidance on credit, market, operational and fraud risks. The Bank is confident in its capacity to absorb challenges and effectively navigate the dynamic business environment.

Market risk is managed through Basel ratios, the Internal Capital Adequacy Assessment, behavioural studies and stress testing. The Bank ensures full compliance with SBP's instructions for implementing International Financial Reporting Standard (IFRS) 9.

Our Asset Liability Management, Liquidity Strategy and Contingency Funding Plan guarantee timely liquidity while optimizing profitability. The Asset Liability Committee oversees the management of assets and liabilities.

Operational risk is mitigated through comprehensive data collection, including operational losses, near-miss events, control breaches and risk control exercises. Business continuity and disaster recovery plans are regularly reviewed, with staff training focused on enhancing risk awareness.

Fraud risk is proactively managed by a dedicated 24/7 fraud detection unit, monitoring digital banking transactions. IT security risks are addressed with automated solutions, regular risk assessments, access reviews and continuous monitoring through a 24/7 Security Operations Centre.

Shari'ah Non-Compliance Risk is carefully managed under the oversight of the Shari'ah Board, Shari'ah Compliance Department, Shari'ah Audit Department and the Shari'ah Non-Compliance Risk Management Committee, ensuring full adherence to Shari'ah principles.

Statement on Internal Control

The Board fully supports management's statement on internal controls, including the assessment of Internal Control over Financial Reporting (ICFR). Management's detailed Statement on Internal Control is included in the Annual Report.

Statement under Code of Corporate Governance and Section 227 of Companies Act 2017

The Board is fully committed to ensuring compliance with the Corporate Governance requirements set forth by the Securities and Exchange Commission of Pakistan. The Bank adheres to sound governance practices and the Directors are pleased to report the following:

- The financial statements accurately represent the Bank's state of affairs, operations, cash flows and changes in equity.
- Proper books of accounts have been diligently maintained.
- Consistent application of appropriate accounting policies in financial statement preparation, with reasonable and prudent judgment in accounting estimates.
- Adherence to International Financial Reporting Standards applicable to banks in Pakistan, with any deviations adequately disclosed.
- No material departure from best practices of Corporate Governance.
- No significant doubts about the Bank's ability to continue as a going concern.
- Transfer of Rs. 847.73 million profit to Statutory Reserve for the year 2024.
- A soundly designed and effectively implemented Internal Control System.

- MCB Bank Limited (Parent Bank) holding 1,554,999,993 shares of the Bank as of December 31, 2024, with non-executive directors holding 07 shares each.
- Statement of Compliance with Code of Corporate Governance included in the Annual Report.
- Composition of the Board is detailed in the Corporate Governance Section.
- Committees of the Board and their Terms of Reference disclosed separately.
- Details of Board and committee meetings, including attendance by each Director, disclosed in the Corporate Governance Section.
- Names of individuals who were directors during the financial year disclosed in the Corporate Governance Section.
- Details of remuneration of Chairman, President/CEO and Non-Executive Directors, including independent Directors, disclosed in note 39 of the financial statements.
- Non-executive directors receive reasonable remuneration for attending meetings, ensuring independence.
- No fee is paid to Directors who do not attend meetings and no fee for resolutions considered through circulation.
- Details of directors' training programs outlined in the Statement of Compliance with the Code of Corporate Governance.
- Key operating and financial data for the last five years presented in the Annual Report.
- The Provident Fund's investment value, based on unaudited accounts as of December 31, 2024, stands at Rs. 854.7 million.
- No overdue statutory payments for taxes, duties, levies, or charges.

Charity Funds Management

Charity is a fundamental pillar in fostering a thriving society and the Bank remains committed to giving back, in line with the Islamic principle of Ihsan, both directly and indirectly.

To prevent misuse, customers are required to contribute to a charity account in the case of late payments. Furthermore, during Shari'ah audits, if any transaction deviates from the established Shari'ah compliance guidelines, the income from such transactions is directed to the charity account. In 2024, Rs. 21.5 million was disbursed from the charity account on behalf of customers to support various charitable organizations, as detailed in Note 21.2 of the Financial Statements.

Trading of Shares of the Bank

The Bank is presently a non-listed entity; therefore, no transactions involving the shares of the Bank were executed by the Directors, executives, or their spouses and minor children during the year 2024.

Auditors

The outgoing auditors, M/s. A. F. Ferguson & Co., Chartered Accountants, who are eligible for reappointment, have expressed their willingness to continue for the next term. Following the Audit Committee's recommendations, the Board endorses the reappointment of M/s. A. F. Ferguson & Co., Chartered Accountants, as the statutory auditors for the financial year ending December 31, 2025.

Future Outlook

The global economy demonstrated resilience in 2024, with inflation easing globally, although at an uneven pace. While advanced economies are approaching their target inflation levels, several emerging markets and developing economies (EMDEs) continue to face persistent inflationary pressures. However, downside risks remain, including heightened policy uncertainty, shifting trade policies, escalating geopolitical tensions, persistent inflationary pressures and climate-related challenges. These risks pose heightened vulnerabilities, particularly for low-income economies. Navigating these challenges will require decisive global and national policy measures, focusing on safeguarding trade, addressing debt vulnerabilities and promoting investments in human capital and infrastructure. The IMF projects a decline in global headline inflation to 4.2% in 2025, down from 5.7% in 2024. Meanwhile, global growth forecasts from the IMF and World Bank stand at 3.3%

[2024: 3.2%] and 2.7% [2024: 2.7%] for 2025, indicating modest but stable economic expansion.

Pakistan's economic outlook remains cautiously optimistic, contingent on the timely resolution of key structural challenges. The declining inflation is expected to stimulate industrial activity, while reduced economic uncertainty could strengthen business and investor confidence, driving higher investment inflows. However, despite the continued stabilization of macroeconomic indicators, fiscal and monetary policies are expected to remain measured and prudent. The government's efforts to support farmers through modernization and innovative agricultural practices aim to enhance crop production levels, though weather-related risks remain a key concern. Comprehensive reforms in the energy sector, public institutions and climate resilience are critical for sustaining long-term economic stability. The IMF projects Pakistan's GDP growth to rise from 2.5% in 2024 to 3.0% in 2025, reflecting a gradual recovery.

The banking sector is facing increasing risks, particularly in the areas of credit, operations and cybersecurity, driven by the rapid growth of digital financial services. To mitigate these risks, the sector must adopt a robust and proactive approach to strategic risk management. In line with these evolving challenges, the SBP has recently revised its guidelines on Profit & Loss Distribution and Pool Management. The updated regulations mandate that Islamic banks must ensure a minimum profit of 75% on Rupees savings deposits (excluding those from financial institutions, public sector enterprises and public limited companies) relative to the weighted average gross yield of all pools. While these changes aim to improve transparency and better align depositors' returns with market performance, they present short-term profitability challenges for the Islamic banking sector.

Despite the challenges ahead, we remain steadfast in our commitment to sustainable growth. Our strategy focuses on enhancing profitability through the acquisition of cost-effective deposits, optimizing asset management and accelerating our digital transformation. We are also investing in robust IT infrastructure, prioritizing employee satisfaction and adopting best-in-class management practices. With a forward-thinking approach, we are well-equipped to navigate the evolving banking landscape, maintain our leadership position and continue thriving.

Acknowledgment

On behalf of the Board and management, we express our sincere gratitude to our valued customers, esteemed business partners and shareholders for their continued trust and support. We also appreciate the guidance provided by the State Bank of Pakistan, the Securities & Exchange Commission of Pakistan, other regulatory authorities and our Shari'ah Board. Furthermore, we commend the dedication of our staff, whose exceptional efforts have been instrumental in driving the growth of our franchise, even amidst challenging business conditions.

For and on behalf of the Board of Directors

Zargham Khan Durrani
President / CEO

Raza Mansha
Chairman