Internship Report
on
Credit Performance Analysis of Al-Arafah Islami Bank PLC

Submitted To:

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Department of Business Administration

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Daffodil International University

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Letter of Transmittal

Ms. Rozina Akter
Assistant Professor
Department of Business Administration
Faculty of Business and Entrepreneurship
Daffodil International University

Subject: Submission of Internship Report on "Credit Performance Analysis of Al-Arafah Islami Bank PLC"

Dear Ma'am,

It is a great honor and privilege for me to submit my internship report titled **"Credit Performance Analysis of Al-Arafah Islami Bank PLC"** as part of the requirement for completing my Bachelor of Business Administration (BBA) program under the Department of Business Administration, Faculty of Business & Entrepreneurship.

This report aims to evaluate the credit performance of Al-Arafah Islami Bank PLC over the past five years (2019 – 2023). It highlights the bank's credit policies, performance indicators, and potential challenges, offering recommendations to address the identified issues. The preparation of this report has been a valuable learning experience that has significantly enhanced my understanding of Islamic banking and finance.

I have prepared this report with utmost sincerity and care. Thank you for your constant guidance and support throughout the preparation of this report. I am truly grateful for your mentorship and the opportunity to learn under your supervision.

Sincerely yours,

Shoumyajit

Shoumyajit Sarkar
ID: 201-11-943
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Department of Business Administration
Faculty of Business & Entrepreneurship
Daffodil International University

Certificate of Approval

This is to certify that the internship report titled **"Credit Performance Analysis of Al-Arafah Islami Bank PLC"**, submitted by **Shoumyajit Sarkar**, bearing Student ID: **201-11-943**, is prepared in partial fulfillment of the requirements for the Bachelor of Business Administration (BBA) program under the Department of Business Administration, Faculty of Business & Entrepreneurship, Daffodil International University.

I hereby recommend this report for submission and acceptance.

Rozina Akter

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Ms. Rozina Akter
Assistant Professor
Department of Business Administration
Faculty of Business and Entrepreneurship
Daffodil International University
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Declaration

I, **Shoumyajit Sarkar**, bearing Student ID: **201-11-943,** a student of the Bachelor of Business Administration (BBA) program under the Department of Business Administration, Faculty of Business & Entrepreneurship, Daffodil International University, hereby declare that the internship report titled **"Credit Performance Analysis of Al-Arafah Islami Bank PLC"** has been prepared solely by me.

I further declare that this report is my original work, and it has not been submitted to any other institution or organization for academic or professional purposes. Any information or data borrowed from external sources has been duly acknowledged.

Sincerely yours,

Shoumyajit

Shoumyajit Sarkar
ID: 201-11-943
Program: BBA, Major in Finance
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Acknowledgment

First and foremost, I am profoundly grateful to Almighty Allah for granting me the strength and ability to complete this internship report titled **"Credit Performance Analysis of Al-Arafah Islami Bank PLC."**

I express my heartfelt gratitude to my academic supervisor, **Ms. Rozina Akter**, Assistant Professor, Department of Business Administration, Faculty of Business & Entrepreneurship, Daffodil International University, for her continuous guidance, encouragement, and invaluable advice throughout this internship and the preparation of this report.

I would also like to extend my sincere thanks to the management and staff of Al-Arafah Islami Bank PLC for providing me with the opportunity to complete my internship in their esteemed organization. Their support and cooperation allowed me to gain practical knowledge and insights into Islamic banking operations.

Lastly, I am grateful to my family, friends, and peers, whose unwavering support and encouragement have been instrumental in completing this work successfully.

Executive Summary

This report, titled **“Credit Performance Analysis of Al-Arafah Islami Bank PLC”**, evaluates the bank’s credit policies and procedures, assesses its financial performance over the last five years (2019-2023), and identifies key challenges and areas for improvement. The report aims to provide insights into the effectiveness of Al-Arafah Islami Bank's credit operations and highlight strategies to enhance its financial performance moving forward.

The study begins by examining the existing credit policies and procedures of Al-Arafah Islami Bank, including its credit approval process, risk management strategies, and Shariah compliance. It then delves into a quantitative analysis of the bank’s credit performance over the five-year period, using key financial ratios such as the Non-Performing Loan (NPL) ratio, Credit to Deposit Ratio (CDR), Return on Assets (ROA), and Loan Loss Provision (LLP) ratio, among others. The analysis reveals both strengths and weaknesses in the bank’s credit operations.

Key findings from the financial analysis include an increasing trend in classified loans, which peaked in 2021, and the bank's proactive approach to provisioning for both unclassified and classified loans. Despite these provisions, the bank faces challenges in reducing its NPL ratio and improving profitability indicators like ROA and ROE.

The report also identifies major challenges such as the rising levels of classified loans, a slight decrease in ROA and ROE, and a growing reliance on debt financing. Recommendations are provided to address these issues, focusing on improving loan portfolio quality, enhancing risk management strategies, and optimizing profitability through better asset utilization.

Overall, this report provides a comprehensive overview of Al-Arafah Islami Bank's credit performance and offers actionable insights to improve its credit operations, financial stability, and long-term profitability.

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Chapter-1

Introduction

1.1: Introduction

The banking sector plays a pivotal role in the economic development of any country, and in Bangladesh, Islamic banking has gained significant traction in recent years. Al-Arafah Islami Bank PLC, as a leading institution in the Islamic banking industry, has been at the forefront of offering Shariah-compliant financial services. This report, titled **"Credit Performance Analysis of Al-Arafah Islami Bank PLC,"** aims to provide a comprehensive evaluation of the bank's credit policies, its performance over the past five years, and the challenges it faces in maintaining a robust financial position.

The primary objective of this report is to analyze the existing credit policies and procedures implemented by Al-Arafah Islami Bank, assess the credit performance using various financial ratios, and identify potential areas of improvement. The report will further examine how the bank has managed its credit portfolio in alignment with Shariah principles while meeting the demands of its customers.

Credit management is one of the most critical aspects of any bank's operation. Effective credit policies ensure that the bank can lend prudently, minimize risks, and achieve sustainable growth. For Islamic banks like Al-Arafah Islami Bank, this responsibility is even more crucial, as they must adhere to the principles of Islamic finance, avoiding interest-based transactions and ensuring compliance with ethical standards.

This report will analyze the bank's credit performance over the past five years (2019-2023) by utilizing key financial to evaluate how effectively the bank has managed its credit portfolio. The findings of this report will help in identifying any gaps or issues related to the bank's credit management and will provide recommendations to improve its performance and strengthen its market position.

1.2: Background of the Study

As a Bachelor of Business Administration (BBA) student at Daffodil International University, I had the opportunity to complete my mandatory internship at Al-Arafah Islami Bank PLC, one of the leading Islamic banks in Bangladesh. Under the supervision of my academic advisor, Ms. Rozina Akter, Assistant Professor in the Department of Business Administration, I focused on analyzing the bank's credit performance over the past five years (2019-2023). During my internship, I gained firsthand experience in understanding the bank's credit policies and their impact on overall financial performance.

The primary objective of my internship was to assess the effectiveness of Al-Arafah Islami Bank’s credit management strategies, particularly in the context of Islamic banking principles. I had the chance to observe how the bank adheres to Shariah-compliant practices while managing its credit portfolio, and how it balances profitability with risk management. This experience allowed me to explore various credit risk management frameworks used by the bank, including credit assessment, monitoring, and recovery procedures.

Through this internship, I acquired valuable insights into the operational challenges and opportunities faced by Al-Arafah Islami Bank in managing its credit portfolio. The hands-on experience helped me understand the intricacies of Islamic financing models and how they are applied in real-world banking. Additionally, I was able to observe the impact of macroeconomic factors and market trends on the bank's credit performance, providing me with a practical understanding of the financial and operational dynamics that drive a bank's success.

This internship was not only a crucial part of my academic journey but also a significant opportunity for my professional growth. It enhanced my understanding of credit management within the framework of Islamic banking and gave me a deeper appreciation of how effective credit policies can contribute to the stability and growth of a financial institution.

1.3: Objective of the Study

The objectives of my study are as follows:

1. To evaluate the existing credit policies and procedures implemented by Al-Arafah Islami Bank PLC.
2. To assess the previous 5 (2019-2023) years credit performance by using different types of ratios.
3. To identify the problems related to the financial performance of Al-Arafah Islami Bank PLC.
4. To provide recommendations for addressing the identified problems.

1.4: Scope of the Study

This study focuses on evaluating the credit performance of Al-Arafah Islami Bank PLC from 2019 to 2023. It covers an analysis of the bank's credit policies, procedures, and overall credit management practices in alignment with Islamic banking principles. The study will assess the bank's credit performance through key financial ratios, identify challenges in managing credit risk, and propose recommendations for improving its credit portfolio and profitability. The research is based on secondary data, including the bank's financial statements and reports, and is limited to Al-Arafah Islami Bank PLC.

1.5: Methodology of the Study

This study primarily relies on secondary data to analyze the credit performance of Al-Arafah Islami Bank PLC. The data used in this report has been sourced from the bank's annual reports, financial statements, and other publicly available documents from the bank's official website and relevant industry publications. Key financial ratios, including the Non-Performing Loan (NPL) ratio and credit-to-deposit ratio, will be used to evaluate the bank's credit performance over the five-year period from 2019 to 2023. The methodology focuses on qualitative and quantitative analysis to assess the effectiveness of the bank's credit policies and management practices.

1.5.1: Sources of Data Collection

The data for this study has been collected from **secondary sources**, including:

- **Annual Reports** of Al-Arafah Islami Bank PLC (2019-2023), which provide detailed financial statements and insights into the bank's operations, credit policies, and performance.
- **Financial Statements** (Balance Sheets, Profit and Loss Statements, and Cash Flow Statements) from the bank's official publications, which are crucial for evaluating financial ratios.
- **Official Website** of Al-Arafah Islami Bank PLC, which contains relevant data, reports, and updates on the bank's activities and performance.
- **Research Papers** and **articles** on Islamic banking and credit management practices to support theoretical and practical understanding.

1.5.2: Limitations of the Study

This study is subject to certain limitations, including:

1. **Data Availability**: The analysis is based solely on secondary data, primarily from the bank's public reports, which may not provide complete or real-time information on internal processes or decision-making.
2. **Lack of Primary Data**: The study does not include primary data collected through surveys or interviews with bank officials or customers, which could have provided deeper insights into the practical challenges faced in credit management.
3. **Time Constraints**: Due to the limited time frame of the internship, the analysis focuses on a specific five-year period (2019-2023), which may not fully capture long-term trends or shifts in the bank's credit performance.
4. **Generalization**: The findings are limited to Al-Arafah Islami Bank PLC and may not be generalized to other banks in Bangladesh, as different banks may have varying credit management practices and policies.
5. **External Factors**: The study does not account for external factors such as regulatory changes, economic conditions, or global financial events that may have impacted the bank's credit performance.

Chapter-2
Overview of Al-Arafah Islami Bank PLC

2.1: Introduction of the Company

Al-Arafah Islami Bank PLC is one of the leading private sector banks in Bangladesh, founded in 1995. As a prominent Islamic bank, it operates under the principles of Islamic Shariah, providing a wide range of financial products and services that comply with Islamic law. The bank offers services in retail banking, corporate banking, SME (Small and Medium Enterprises) banking, and Islamic capital markets. Its core offerings include deposit schemes, investment products, and financing services, all structured according to Islamic financial principles such as Murabaha, Mudaraba, Musharaka, and Ijara.

The bank was established with the aim of meeting the growing demand for Shariah-compliant financial services in Bangladesh. Over the years, Al-Arafah Islami Bank has gained a strong reputation for its commitment to ethical banking practices, customer-centric services, and its role in promoting financial inclusion. It has successfully integrated technology to enhance its services, offering online banking facilities, mobile banking, and other digital services to its customers.

Headquartered in Dhaka, the bank operates a wide network of branches across the country, providing accessible banking solutions to individuals, businesses, and communities. Al-Arafah Islami Bank also emphasizes corporate social responsibility (CSR) by contributing to social and economic development through various programs and initiatives aimed at improving education, healthcare, and welfare.

As of today, the bank stands as a key player in the Islamic banking sector in Bangladesh, with a strong customer base, a diverse portfolio of services, and a significant market presence.

2.2: Mission and Vision of Al-Arafah Islami Bank PLC

2.2.1: Mission

The mission of Al-Arafah Islami Bank PLC is to provide innovative, customer-friendly, and Shariah-compliant financial solutions that contribute to the economic development of Bangladesh. The bank aims to ensure the highest standards of financial ethics, maintaining a strong commitment to serving its clients while promoting social responsibility. It strives to create value for its stakeholders, including customers, employees, shareholders, and the broader community, by offering financial products that align with Islamic values and support the nation's sustainable growth.

2.2.2: Vision

The vision of Al-Arafah Islami Bank PLC is to become the most preferred Islamic bank in Bangladesh, known for its excellence in customer service, product innovation, and commitment to Shariah-compliant banking practices. The bank envisions expanding its presence both nationally and internationally while adhering to Islamic principles in every aspect of its business. It seeks to build long-term relationships with customers by offering reliable financial solutions that foster trust, security, and prosperity.

2.3: Objectives of Al-Arafah Islami Bank PLC

- ✓ **To Provide Shariah-Compliant Services**: Offering financial products and services that strictly adhere to Islamic principles.
- ✓ **To Ensure Customer Satisfaction**: Delivering high-quality, customer-focused banking solutions.
- ✓ **To Contribute to Economic Development**: Supporting various sectors such as trade, industry, agriculture, and SMEs through financing.
- ✓ **To Maintain Financial Stability**: Ensuring strong financial health through effective risk management and capital growth.
- ✓ **To Promote Social Responsibility**: Engaging in corporate social responsibility (CSR) initiatives for societal development.

2.4: Government Affiliation

Al-Arafah Islami Bank PLC is a private sector bank in Bangladesh, and while it operates independently, it is regulated by the Bangladesh Bank, the central bank of the country. As a financial institution, it must adhere to the rules and regulations set forth by Bangladesh Bank, including those related to banking operations, monetary policies, and financial reporting. Additionally, Al-Arafah Islami Bank complies with the Bangladesh Securities and Exchange Commission (BSEC) regulations for its listed activities and corporate governance.

Furthermore, the bank follows the guidelines set by the Shariah Supervisory Board, which ensures that its financial products and services are in line with Islamic banking principles. Although the bank is not directly owned or controlled by the government, its operations are closely supervised by regulatory bodies to ensure compliance with national laws and standards.

2.5: Global Partners

Al-Arafah Islami Bank PLC maintains several global partnerships to enhance its international banking capabilities and expand its reach. Some of its notable global partners include:

1. **Correspondent Banks**: Al-Arafah Islami Bank has established strong correspondent banking relationships with international financial institutions to facilitate smooth international transactions, including remittance services, foreign trade, and cross-border payments.
2. **SWIFT Network**: The bank is a member of the Society for Worldwide Interbank Financial Telecommunication (SWIFT**)**, enabling it to securely and efficiently conduct international fund transfers and payments with financial institutions worldwide.
3. **International Trade Partners**: Al-Arafah Islami Bank collaborates with international trade finance organizations to provide financing for global trade, supporting both importers and exporters in Bangladesh.

2.6: Managerial Body of Al-Arafah Islami Bank PLC

The Managerial Body of Al-Arafah Islami Bank PLC consists of a team of experienced professionals responsible for overseeing the bank’s operations, strategic planning, and decision-making processes. The management structure is composed of several key positions, including:

1. **Board of Directors**: The Board of Directors is the highest governing body of the bank, responsible for setting strategic goals, ensuring regulatory compliance, and overseeing the overall performance of the bank. The Board includes influential individuals from diverse sectors, providing governance and strategic direction.
2. **Chief Executive Officer (CEO)**: The CEO leads the day-to-day operations of the bank, implementing the strategies set by the Board of Directors. The CEO is responsible for ensuring the smooth functioning of all departments, managing staff, and making key operational decisions.
3. **Senior Management**: The senior management team includes heads of various departments such as finance, operations, risk management, credit, and marketing. They report directly to the CEO and are responsible for the execution of policies, managing departmental functions, and ensuring operational efficiency.
4. **Shariah Supervisory Board**: Given the bank's Islamic banking operations, the Shariah Supervisory Board plays a vital role in ensuring that all financial products and services are in compliance with Islamic principles. The board consists of scholars and experts in Islamic finance who guide the bank's operations.
5. **Branch Managers**: The branch managers oversee the operations of individual branches, ensuring that services are delivered in accordance with the bank's policies and objectives.

2.7: Strength of Al-Arafah Islami Bank PLC

Al-Arafah Islami Bank PLC has several key strengths that contribute to its success and growth in the competitive banking sector:

- ✓ **Shariah-Compliant Banking**: As a fully Islamic bank, Al-Arafah Islami Bank is committed to offering services that strictly adhere to Islamic principles, which appeals to a large segment of the population in Bangladesh seeking ethical banking solutions.
- ✓ **Strong Financial Position**: The bank has consistently demonstrated strong financial performance, with solid asset growth, profitability, and a stable capital base. This enables it to maintain resilience during market fluctuations and continue expanding its services.
- ✓ **Wide Network of Branches**: Al-Arafah Islami Bank operates a large network of branches across Bangladesh, ensuring broad accessibility to its services for individuals, businesses, and communities, particularly in rural and underserved areas.

- ✓ **Diversified Product Portfolio**: The bank offers a wide range of Shariah-compliant financial products including savings accounts, investment products, trade finance, and SME financing. This diversity helps the bank cater to the varying financial needs of its customers.
- ✓ **Experienced Management Team**: With a seasoned and skilled management team, Al-Arafah Islami Bank is able to make informed decisions and effectively steer the bank towards sustainable growth and innovation in Islamic banking.
- ✓ **Technological Integration**: The bank has embraced digital banking solutions, offering online banking, mobile apps, and other digital services, which enhance customer experience and operational efficiency.
- ✓ **Corporate Social Responsibility (CSR)**: Al-Arafah Islami Bank is also committed to social welfare, contributing to various CSR initiatives, including education, healthcare, and community development, which helps build a positive brand image.

2.8: Challenges Faced by Al-Arafah Islami Bank PLC

- ➢ **Intense Competition**: The bank faces strong competition from both conventional and Islamic banks in Bangladesh, which challenges its ability to differentiate its offerings and retain market share.
- ➢ **Non-Performing Loans (NPLs)**: Managing the growing issue of non-performing loans remains a significant challenge, as it directly impacts the bank's financial stability and profitability.
- ➢ **Regulatory Compliance**: Adapting to changing regulations from Bangladesh Bank and ensuring adherence to Shariah principles adds complexity to the bank's operational processes.
- ➢ **Economic Volatility**: The unpredictable nature of the national economy, including inflation, exchange rate fluctuations, and economic recessions, poses a risk to the bank’s overall performance.
- ➢ **Technology Integration and Cybersecurity**: While digital banking is growing, the bank must continuously invest in new technologies and ensure robust cybersecurity measures to protect customer data and maintain trust.
- ➢ **Liquidity Management**: Balancing liquidity needs with compliance to Islamic banking principles is a challenge, particularly when managing large-scale withdrawals or long-term investments.

- **Managing Islamic Banking Risks**: The bank must carefully balance Shariah-compliant financing with risk management practices, requiring specialized knowledge and expertise in Islamic finance.

2.9: Facilities Offred by G Al-Arafah Islami Bank PLC

- ✓ **Shariah-Compliant Deposit Accounts**: Mudaraba Savings and Term Deposit Accounts.
- ✓ **Retail Banking Services**: Personal, home, education, and car loans based on Islamic financing.
- ✓ **Islamic Trade Finance**: Letters of Credit, Trade Financing, and other import/export services.
- ✓ **SME Financing**: Specialized financing solutions for small and medium-sized enterprises.
- ✓ **Islamic Investment Products**: Mudaraba and Musharaka-based investment opportunities.
- ✓ **Online Banking Services**: Convenient access to banking through internet and mobile banking.
- ✓ **ATM and Debit Cards**: Easy access to funds and payments through ATM/debit cards.
- ✓ **Islamic Capital Market Services**: Investment in Sukuk and Shariah-compliant securities.
- ✓ **Remittance Services**: Domestic and international money transfer facilities.
- ✓ **Foreign Exchange Services**: Currency exchange and support for international transactions.

2.10: Accounts offered by Al-Arafah Islami Bank PLC

- **Mudaraba Savings Account**: A Shariah-compliant savings account where the bank acts as an agent for investing the deposited funds in profit-generating ventures, and the profit is shared according to the agreed ratio between the bank and the customer.
- **Mudaraba Term Deposit Account**: A fixed-term deposit account offering higher profit rates, where the funds are invested in Shariah-compliant ventures for a specified period, and the returns are shared between the bank and the customer.
- **Current Account**: A non-interest-bearing account designed for businesses and

individuals, providing the convenience of conducting frequent transactions without profit-sharing. This account allows easy access to funds, including deposits and withdrawals.

- **Mudaraba Special Savings Account**: A special savings account with higher profit rates compared to regular savings accounts, catering to customers who want to invest their savings for a longer term while adhering to Islamic finance principles.
- **Joint Account**: A Mudaraba-based joint account where two or more individuals can open a savings or term deposit account and share the profit according to their contribution.
- **Student Account**: A tailored savings account designed specifically for students, offering easy access to funds and low minimum balance requirements, while generating profits in line with Islamic principles.
- **Non-Resident Foreign Currency Account (NRB)**: A Shariah-compliant foreign currency account for non-resident Bangladeshis (NRBs), allowing them to manage their foreign currency transactions with ease.
- **Non-Resident Taka Account (NRTA)**: A Shariah-compliant account specifically designed for non-resident Bangladeshis to hold and manage Taka, offering them facilities for remittances and local transactions.

2.11: Services Offred by Al-Arafah Islami Bank PLC

1. **Retail Banking Services**:
    - Personal Loans (Home Loans, Car Loans, Education Loans)
    - Credit Cards and Debit Cards
    - Account Opening and Fund Transfers
2. **Corporate Banking Services**:
    - Business Loans
    - Trade Finance and Working Capital Financing
    - Cash Management Services
3. **Islamic Banking Services**:
    - Murabaha Financing (Cost-Plus Financing)
    - Mudaraba Financing (Profit-Sharing Financing)
    - Musharaka Financing (Partnership Financing)
    - Ijara (Leasing Services)

4. **SME Banking**:
    - Financing for Small and Medium Enterprises
    - Business Advisory Services
    - Working Capital Financing
5. **Online and Mobile Banking**:
    - Internet Banking for fund transfer, bill payments, etc.
    - Mobile Banking for easy access to accounts and services
6. **Foreign Exchange Services**:
    - Currency Exchange for domestic and international transactions
    - Remittance Services for sending and receiving money globally
7. **Trade Finance**:
    - Letter of Credit (LC), Guarantees, and Export Financing
    - Import and Export Services for international business transactions
8. **ATM Services**:
    - Access to ATMs nationwide for cash withdrawals and fund transfers
9. **Wealth Management and Investment**:
    - Investment Products like Sukuk (Islamic bonds)
    - Shariah-compliant investment advisory services
10. **Mobile Financial Services**:
    - Mobile wallet services for sending and receiving money on the go
    - Bill Payments, Mobile Top-Ups, and other mobile banking services

Chapter - 3

Evaluation of Credit Policies & Procedures at Al-Arafah Islami Bank PLC

3.1: Overview of Credit Policies at Al-Arafah Islami Bank PLC

Al-Arafah Islami Bank PLC operates with a well-defined set of credit policies designed to ensure responsible lending practices while adhering to Islamic financial principles. The core focus of these policies is to avoid Riba (interest) and follow Shariah-compliant financing methods such as Murabaha, Mudaraba, and Musharaka, which promote ethical, asset-backed lending and risk-sharing.

The bank's credit policies guide the approval, management, and recovery of loans, aiming to balance risk and profitability. Key to this approach is the Shariah Supervisory Board, which ensures that all credit transactions are aligned with Islamic law, particularly by avoiding interest and speculation.

To manage credit risk, the bank conducts thorough creditworthiness assessments, focusing on the borrower's financial stability, repayment capacity, and the potential risks involved in each loan. Loans are also secured with appropriate collateral when necessary, reducing the risk of defaults. Additionally, the bank diversifies its loan portfolio to minimize sector-specific risks and adopts risk-based pricing for loans.

Continuous monitoring of loans allows the bank to identify potential issues early and take corrective actions such as loan restructuring, if needed. Furthermore, the bank emphasizes ethical financing, ensuring that loans are provided only for projects that align with Islamic values, excluding industries like alcohol, gambling, or tobacco.

In summary, Al-Arafah Islami Bank's credit policies are structured to support sustainable growth, minimize credit risks, and maintain compliance with Islamic finance principles. These policies are regularly reviewed to ensure they remain effective and competitive in the evolving financial landscape.

3.2: Types of Credit Products Offered by Al-Arafah Islami Bank PLC

Al-Arafah Islami Bank offers a wide range of credit products catering to the diverse financial needs of individuals, businesses, and corporations. These products are structured to align with Islamic finance principles, emphasizing ethical financing and risk-sharing.

1. **Personal Loans**: Offered to individuals for personal needs, such as medical expenses or education, structured under Murabaha (cost-plus financing) and Mudaraba (profit-sharing) agreements.
2. **Home Loans**: The bank provides Murabaha-based home loans, where the bank purchases the property and resells it to the borrower at a marked-up price, making it compliant with Islamic finance principles.
3. **Car Loans**: Murabaha-based car loans enable customers to purchase vehicles with flexible repayment terms, ensuring the loan structure adheres to Shariah laws.
4. **SME Loans**: For small and medium-sized enterprises, Al-Arafah Islami Bank offers Mudaraba and Musharaka financing solutions to help businesses with working capital and expansion.
5. **Trade Financing**: The bank provides comprehensive trade finance services, including Letters of Credit (LC), export financing, and import financing, allowing businesses to engage in international trade smoothly.
6. **Corporate Loans**: Large corporations can access both short-term and long-term loans structured under Murabaha, Mudaraba, or Musharaka, providing flexible solutions for business expansion.

3.3: Credit Approval Process

The credit approval process at Al-Arafah Islami Bank is a systematic and multi-step procedure designed to evaluate the borrower’s financial condition, business viability, and adherence to Islamic principles. The steps include:

- **Application Submission**: Customers initiate the process by submitting a detailed application, including required financial documents and the loan’s purpose.

- **Document Collection and Verification**: The bank collects necessary documentation, including income statements, financial reports, property documents, and guarantees. This step is crucial for evaluating the applicant's financial standing.
- **Evaluation of Creditworthiness**: The bank assesses the applicant's creditworthiness by analyzing factors such as income, debt obligations, past loan performance, and overall financial stability, ensuring compliance with Shariah principles.
- **Risk Assessment**: A risk assessment is conducted to evaluate the potential risks associated with lending, including factors such as collateral value, borrower's business industry, and repayment capacity.
- **Credit Committee Review**: After the evaluation, the loan application is reviewed by the bank's **Credit Committee** for a final decision. The committee assesses the loan's risk and ensures the proposed loan structure is in line with the bank's policies.
- **Shariah Compliance Review**: The bank ensures that all credit transactions are reviewed by the Shariah Supervisory Board, which ensures compliance with Islamic law and confirms that no interest (Riba) is involved.

3.4: Credit Risk Management and Mitigation Strategies

Effective credit risk management is at the core of Al-Arafah Islami Bank's operations. The bank employs several strategies to identify, assess, and mitigate credit risk, ensuring financial stability while providing accessible financing to customers:

- **Diversification**: By diversifying its loan portfolio across various sectors, Al-Arafah Islami Bank minimizes concentration risk and reduces the potential impact of sector-specific downturns.
- **Risk-Based Pricing**: The bank applies risk-based pricing to its credit products, adjusting profit margins based on the borrower's risk profile. Higher-risk loans may carry higher returns to compensate for the increased risk of default.
- **Credit Scoring Models**: The bank utilizes sophisticated credit scoring systems to assess the creditworthiness of applicants, ensuring that only qualified borrowers are approved for loans.

- **Collateral Requirements**: The bank emphasizes securing loans with tangible assets such as real estate, vehicles, and business equipment. This reduces the risk to the bank if the borrower defaults on the loan.
- **Loan Monitoring**: Continuous monitoring of loan performance allows the bank to track the borrower's financial health. This early warning system helps identify potential problems and allows for proactive interventions.
- **Loan Restructuring**: When borrowers face difficulties in meeting repayment obligations, the bank provides restructuring options such as extended repayment periods or revised terms to avoid defaults.

3.5: Credit Documentation and Legal Procedures

Al-Arafah Islami Bank adheres to a stringent documentation process to ensure both legal protection and compliance with Islamic finance principles:

- ✓ **Loan Agreements**: All credit products are accompanied by formal loan agreements, detailing the terms, repayment schedule, profit rates, and any penalties for non-payment. The agreements ensure that the bank and the borrower are legally protected.
- ✓ **Collateral Documentation**: The bank ensures that all collateral provided by the borrower is fully documented and legally verified. This includes property deeds, business guarantees, and third-party guarantees.
- ✓ **Shariah Compliance**: In line with Islamic principles, the loan agreement must include a certification of Shariah compliance, confirming that the transaction avoids interest (Riba) and is structured according to Islamic law.
- ✓ **Legal Verification**: The bank ensures that all documents are legally verified under Bangladeshi law to guarantee the enforceability of the loan agreement in case of default.
- ✓ **Default Procedures**: If a borrower defaults on their loan, Al-Arafah Islami Bank follows a structured legal process for recovery. This includes sending reminders, negotiating new terms, or, if necessary, initiating legal action to seize collateral or recover dues.

3.6: Shariah Compliance in Credit Operations

Shariah compliance is a cornerstone of Al-Arafah Islami Bank's credit operations. The bank ensures that all credit products and services are in line with the principles of Islamic finance, which prohibit interest (Riba) and promote ethical financing practices:

- ✓ **Prohibition of Riba**: In place of traditional interest-based lending, the bank uses Islamic financing models such as Murabaha, Mudaraba, and Musharaka to structure its loans.
- ✓ **Shariah Supervisory Board**: The bank has an active Shariah Supervisory Board that reviews and approves all credit transactions, ensuring compliance with Islamic finance principles and practices.
- ✓ **Ethical Financing**: The bank only provides financing for projects and businesses that meet ethical standards, excluding industries such as alcohol, gambling, and tobacco.
- ✓ **Risk Sharing**: In contrast to conventional finance, Islamic finance emphasizes risk-sharing between the bank and its customers. This is evident in financing models like Mudaraba and Musharaka, where profits and risks are shared by both parties.

3.7: Credit Monitoring and Collection Procedures

Al-Arafah Islami Bank employs a rigorous system for monitoring loans and collecting overdue debts to ensure timely repayment and minimize the risk of defaults:

- ➢ **Ongoing Monitoring**: After loan disbursement, the bank continuously monitors the borrower's financial performance through regular reviews and periodic updates. This helps identify potential repayment problems early.
- ➢ **Early Warning System**: The bank uses an early warning system that flags accounts showing signs of financial distress. This allows the bank to take proactive measures before loans become non-performing.
- ➢ **Collection Strategy**: If loans become overdue, the bank has a defined collection process, which includes reminders, renegotiation of repayment terms, and if necessary, legal proceedings to recover outstanding amounts.
- ➢ **Customer Relationship Management**: The bank maintains close relationships with its borrowers, offering flexible solutions such as loan restructuring or deferrals in case of financial difficulties, thus avoiding defaults.

3.8: Impact of Credit Policies on Bank's Financial Performance

The credit policies implemented by Al-Arafah Islami Bank play a critical role in shaping its financial performance. These policies impact the bank's revenue, risk exposure, and overall financial health:

- **Revenue Generation**: The bank generates significant revenue through its Shariah-compliant credit products, such as Murabaha and Mudaraba, by earning a profit margin on the sale or investment.
- **Risk Management**: Effective risk management ensures that the bank's loan portfolio remains healthy and that non-performing loans (NPLs) are minimized, contributing to financial stability.
- **Customer Loyalty**: By offering transparent and ethical financing solutions, Al-Arafah Islami Bank builds trust and loyalty among its customers, leading to long-term business relationships and repeat financing.
- **Financial Stability**: The bank's sound credit policies help it weather economic fluctuations, reducing the risk of defaults and maintaining its financial strength even in challenging times.

3.9: Challenges in Credit Policy Implementation

Despite the strong framework in place, Al-Arafah Islami Bank faces several challenges in implementing its credit policies:

- **Shariah Compliance Challenges**: Ensuring that all loans are in full compliance with Shariah principles is complex, especially in the face of evolving market conditions and customer needs.
- **Economic Volatility**: Changes in the macroeconomic environment, such as inflation or recession, can increase the likelihood of loan defaults, making credit management more difficult.
- **Competition**: The growing competition in the banking sector, particularly from non-Islamic banks and fintech, presents challenges in attracting and retaining customers.

- **Technological Adaptation**: The need to integrate advanced technology in credit processing, risk assessment, and customer service poses a challenge, requiring significant investment in digital infrastructure.
- **Non-Performing Loans**: Managing the risk of non-performing loans (NPLs) continues to be a challenge for the bank, requiring continuous effort in loan monitoring and collection strategies.

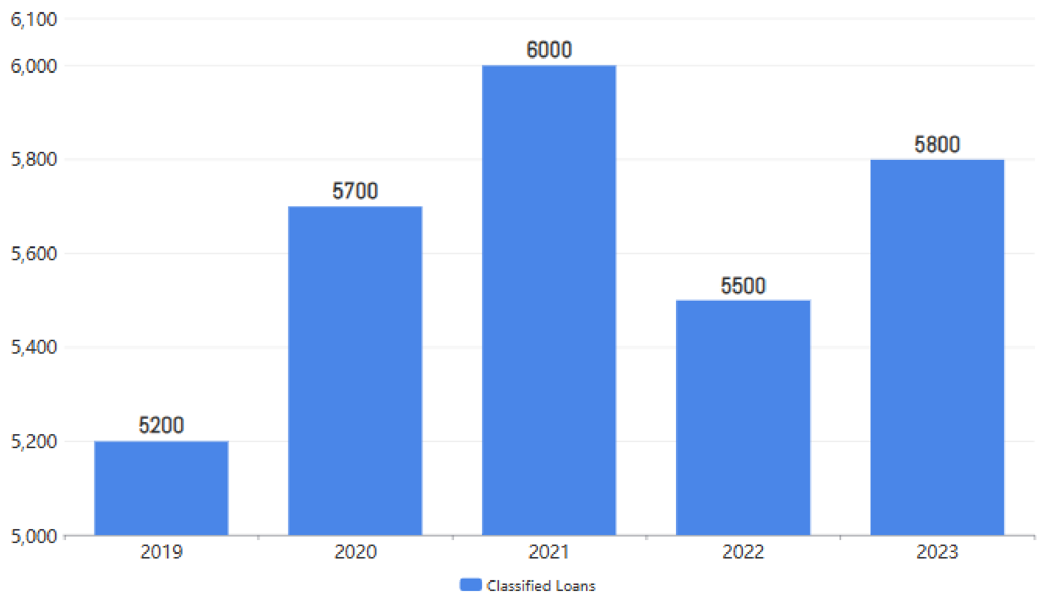
Chapter-4

Credit Performance Analysis of Al-Arafah Islami Bank PLC (2019-2023 Year)

4.1: Classified Loans

Table-1.1: Classified Loans from year 2019-2023

Years	Classified Loans (BDT Million)
2019	5,200
2020	5,700
2021	6,000
2022	5,500
2023	5,800



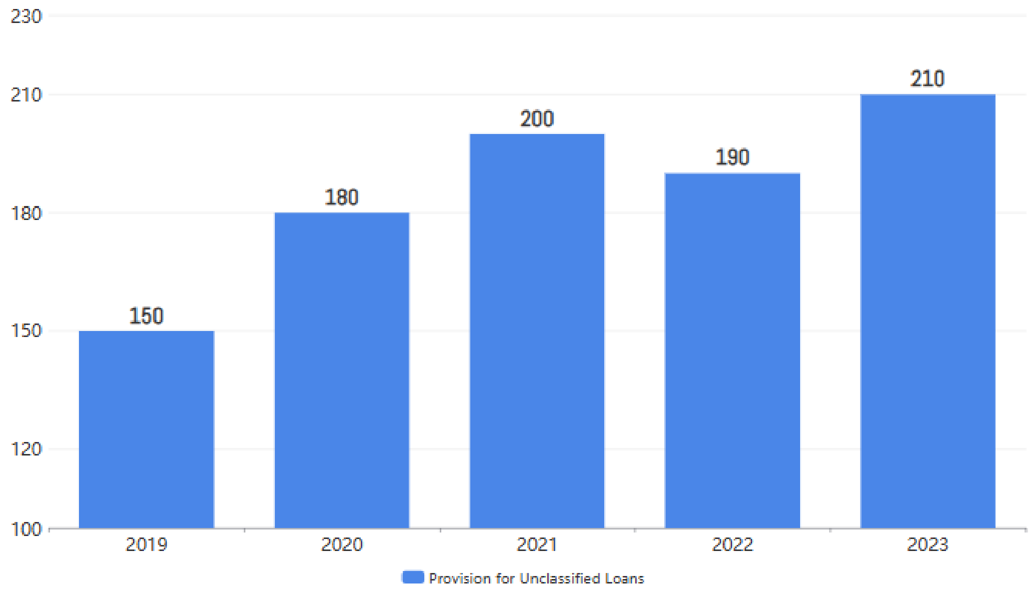
Interpretation:

The Classified Loans of Al-Arafah Islami Bank increased from BDT 5,200 million in 2019 to BDT 6,000 million in 2021, marking a rise over the three years. However, in 2022, it decreased to BDT 5,500 million, before slightly increasing again to BDT 5,800 million in 2023. This fluctuation indicates a rising trend in classified loans, with some recovery in 2022, but the figure remains high, showing continued challenges in managing non-performing loans.

4.2: Provision for Unclassified Loans

Table-1.2: Provision for Unclassified Loans from year 2019-2023

Years	Provision for Unclassified Loans (BDT Million)
2019	150
2020	180
2021	200
2022	190
2023	210



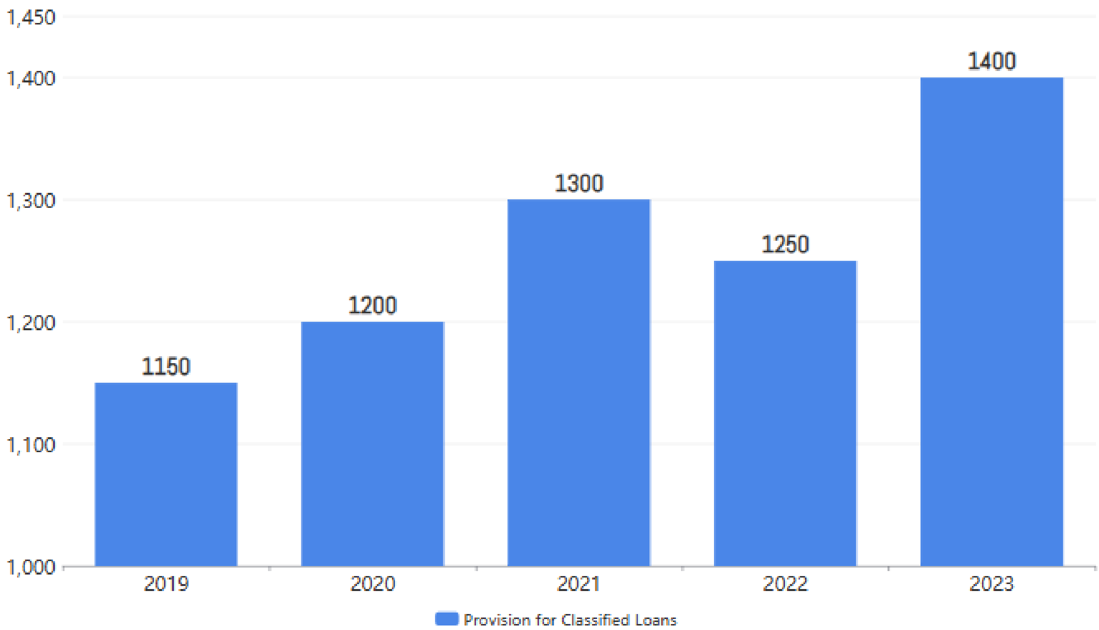
Interpretation:

The Provision for Unclassified Loans increased from BDT 150 million in 2019 to BDT 210 million in 2023, reflecting a steady rise over the five-year period. The provision grew gradually increase from 2019 to 2020, followed BDT 200 million rise in 2021. However, in 2022, it slightly decreased to BDT 190 million but rebounded in 2023. This consistent increase, despite minor fluctuations, suggests that the bank is proactively setting aside more provisions to cover potential risks associated with its unclassified loans.

4.3: Provision for Classified Loans

Table-1.3: Provision for Classified Loans from year 2019-2023

Years	Provision for Classified Loans (BDT Million)
2019	1,150
2020	1,200
2021	1,300
2022	1,250
2023	1,400



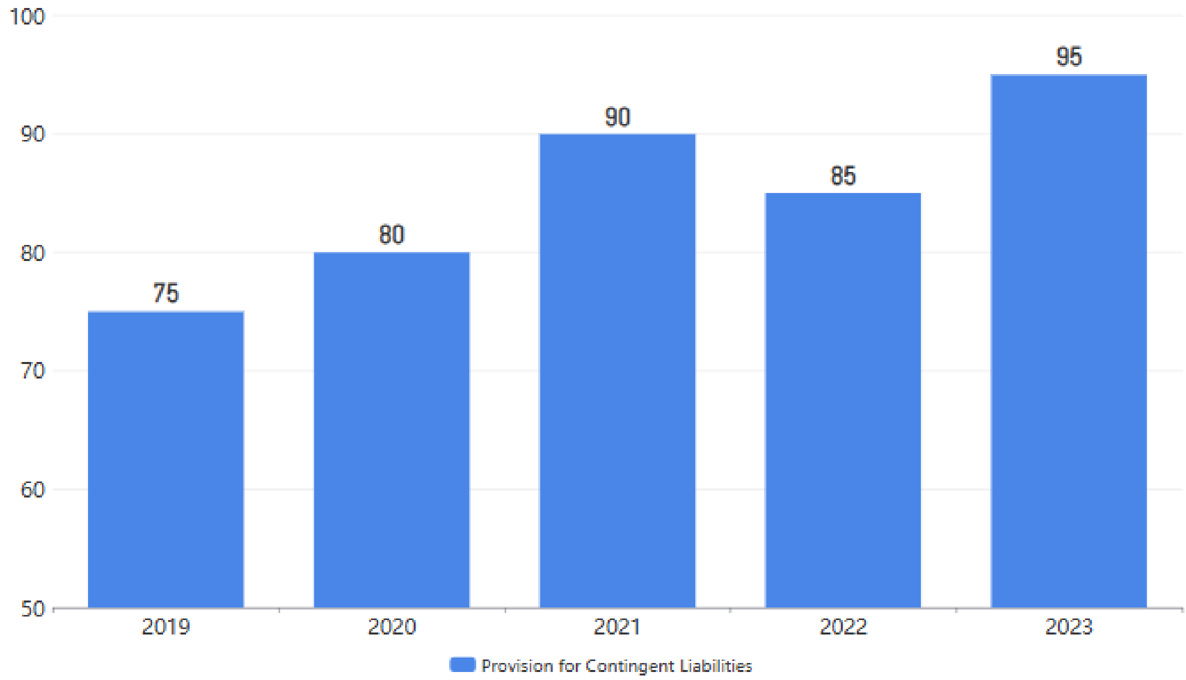
Interpretation:

The Provision for Classified Loans increased from BDT 1,150 million in 2019 to BDT 1,400 million in 2023, reflecting rise over the five-year period. The provision saw consistent growth, with an increase in 2020, followed by BDT 1,300 million rise in 2021. In 2022, it decreased slightly but rebounded in 2023. This upward trend indicates that the bank is strengthening its provisions to cover the growing risks associated with classified loans, highlighting a proactive approach to managing non-performing assets.

4.4: Provision for Contingent Liabilities

Table-1.4: Provision for Contingent Liabilities from year 2019-2023

Years	Provision for Contingent Liabilities (BDT Million)
2019	75
2020	80
2021	90
2022	85
2023	95



Interpretation:

The Provision for Contingent Liabilities increased from BDT 75 million in 2019 to BDT 95 million in 2023, showing a steady rise over the five-year period. The provision grew consistently increase from 2019 to 2020, and further growth in 2021, reaching BDT 90 million. In 2022, it slightly decreased but it increased again in 2023. This trend indicates that the bank has been making prudent provisions to cover potential risks associated with contingent liabilities, ensuring sufficient coverage for possible future obligations.

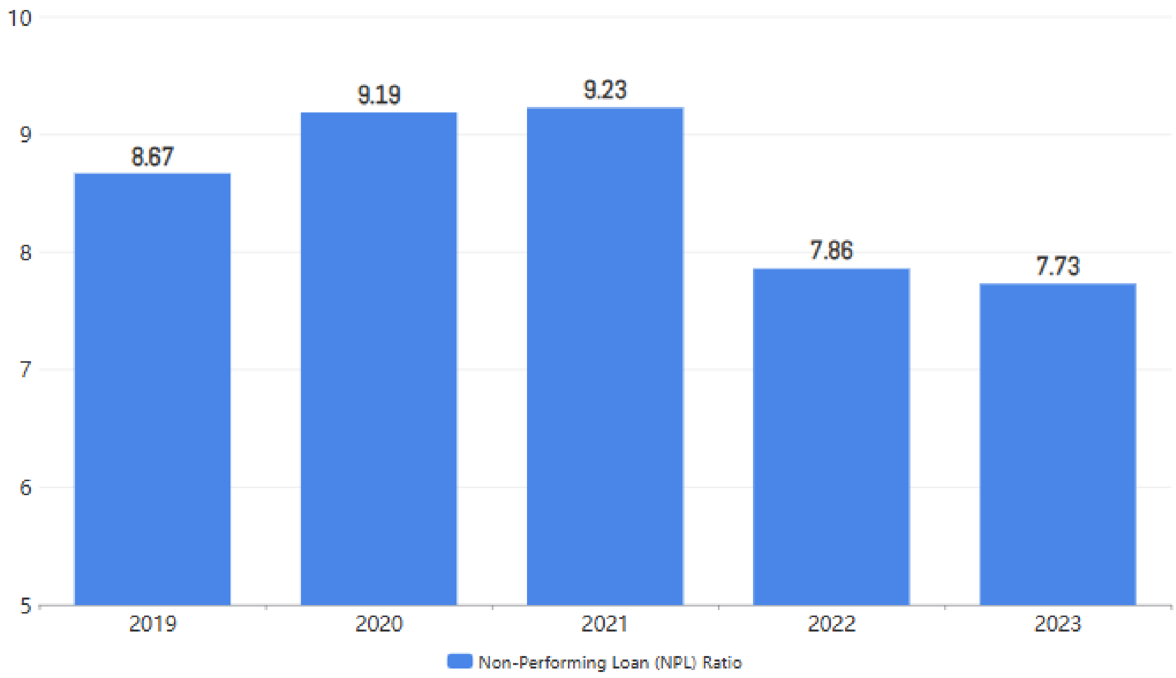
4.5: Non-Performing Loan (NPL) Ratio

To measure the percentage of total loans that are classified as non-performing, indicating the credit quality of the bank.

Formula: $$\text{NPL Ratio} = \left(\frac{\text{Non-Performing Loans}}{\text{Total Loans}}\right) \times 100$$

Table-1.5: NPL Ratio from year 2019-2023

Years	2019	2020	2021	2022	2023
NPL Ratio (%)	8.67	9.19	9.23	7.86	7.73



Interpretation:

The NPL Ratio increased from 8.67% in 2019 to a peak of 9.23% in 2021, reflecting a rise in non-performing loans relative to total loans, possibly due to economic challenges. However, it improved in 2022, dropping to 7.86%, and further to 7.73% in 2023, indicating enhanced credit quality and better recovery efforts by the bank.

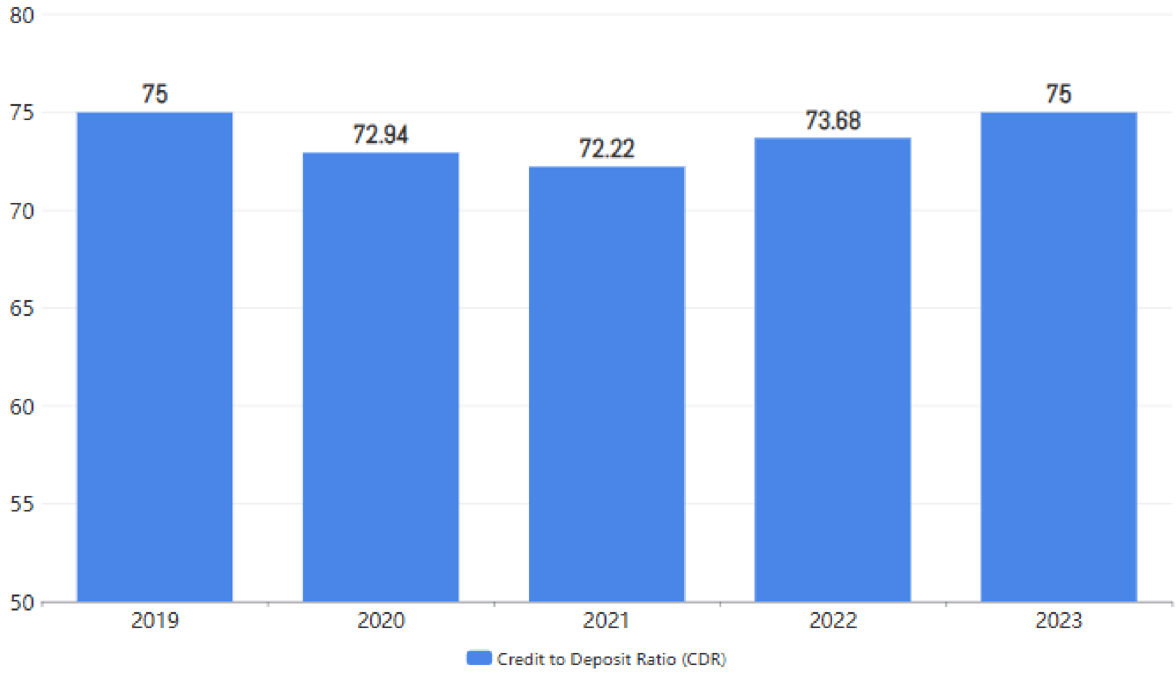
4.6: Credit to Deposit Ratio (CDR)

To assess the bank's efficiency in utilizing customer deposits to generate loans, indicating liquidity and financial health.

Formula: $$\text{CDR} = \left(\frac{\text{Total Loans}}{\text{Total Deposits}} \right) \times 100$$

Table-1.6: Credit to Deposit Ratio (CDR) from year 2019-2023

Years	2019	2020	2021	2022	2023
CDR (%)	75.00	72.94	72.22	73.68	75.00



Interpretation:

The Credit to Deposit Ratio fluctuated slightly, starting at 75.00% in 2019, dropping to 72.22% by 2021 due to a higher growth in deposits relative to loans. It rebounded to 73.68% in 2022 and returned to 75.00% in 2023, indicating stable and efficient utilization of deposits for lending activities over time.

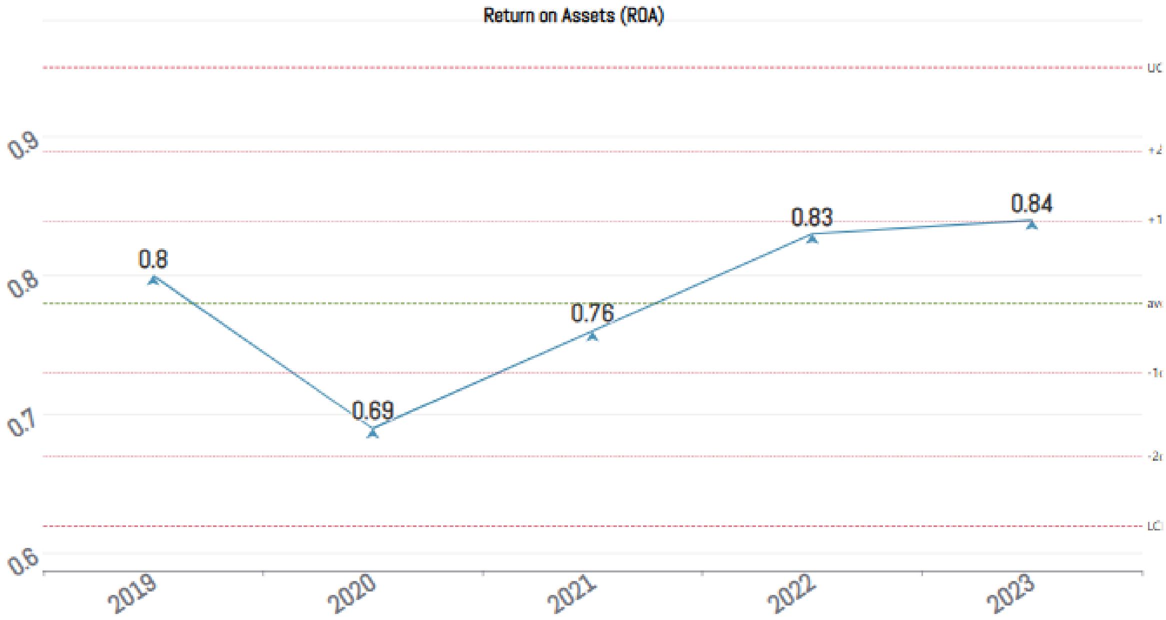
4.7: Return on Assets (ROA)

To measure the bank's profitability in generating net income relative to its total assets, indicating operational efficiency.

Formula: $$\text{ROA} = \left(\frac{\text{Net Income}}{\text{Total Assets}}\right) \times 100$$

Table-1.7: Return on Assets (ROA) from year 2019-2023

Years	2019	2020	2021	2022	2023
ROA (%)	0.80	0.69	0.76	0.83	0.84



Interpretation:

The ROA decreased from 0.80% in 2019 to 0.69% in 2020, likely due to reduced net income during the pandemic. It recovered gradually to 0.83% in 2022 and slightly improved to 0.84% in 2023, reflecting enhanced profitability and efficient asset utilization over time.

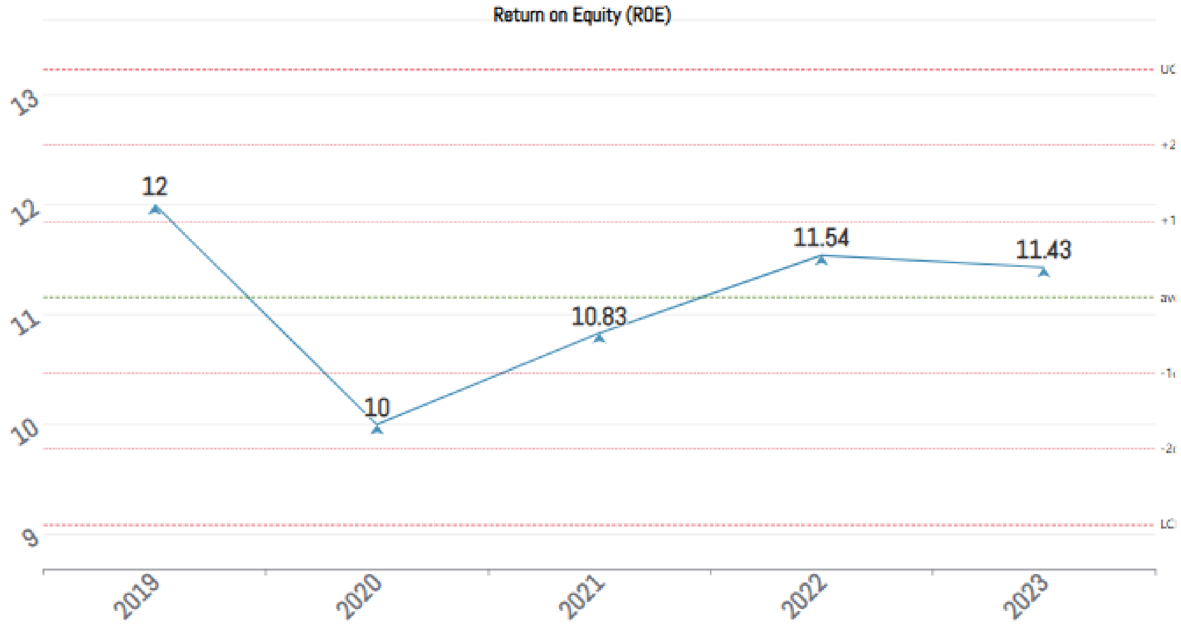
4.8: Return on Equity (ROE)

To measure the bank's profitability by evaluating how effectively it generates net income from shareholders' equity.

Formula: $$\text{ROE} = \left(\frac{\text{Net Income}}{\text{Shareholders' Equity}}\right) \times 100$$

Table-1.8: Return on Equity (ROE) from year 2019-2023

Years	2019	2020	2021	2022	2023
ROE (%)	12.00	10.00	10.83	11.54	11.43



Interpretation:

The ROE decreased from 12.00% in 2019 to 10.00% in 2020, reflecting reduced profitability relative to shareholders' equity during the pandemic. It improved slightly to 11.54% in 2022, before stabilizing at 11.43% in 2023. This trend indicates a gradual recovery in profitability and efficient equity utilization over the five years.

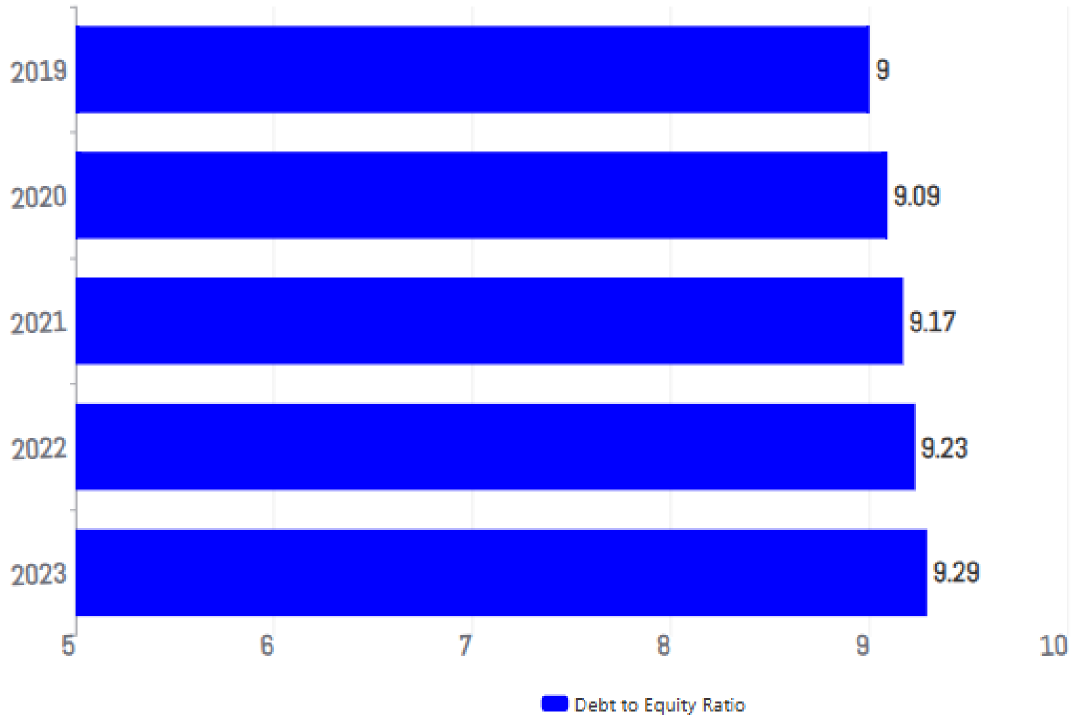
4.9: Debt to Equity Ratio

To evaluate the bank's financial leverage by comparing its total debt to shareholders' equity, indicating the risk level associated with its capital structure.

Formula: $$\text{Debt to Equity Ratio} = \frac{\text{Total Debt}}{\text{Shareholders' Equity}}$$

Table-1.9: Debt to Equity Ratio from year 2019-2023

Years	2019	2020	2021	2022	2023
Debt to Equity Ratio	9.00	9.09	9.17	9.23	9.29



Interpretation:

The Debt-to-Equity Ratio increased slightly over the five-year period, from 9.00 in 2019 to 9.29 in 2023. This gradual rise indicates that the bank has been increasingly relying on debt financing relative to its equity. While such a trend supports growth, it also highlights higher financial leverage and associated risks.

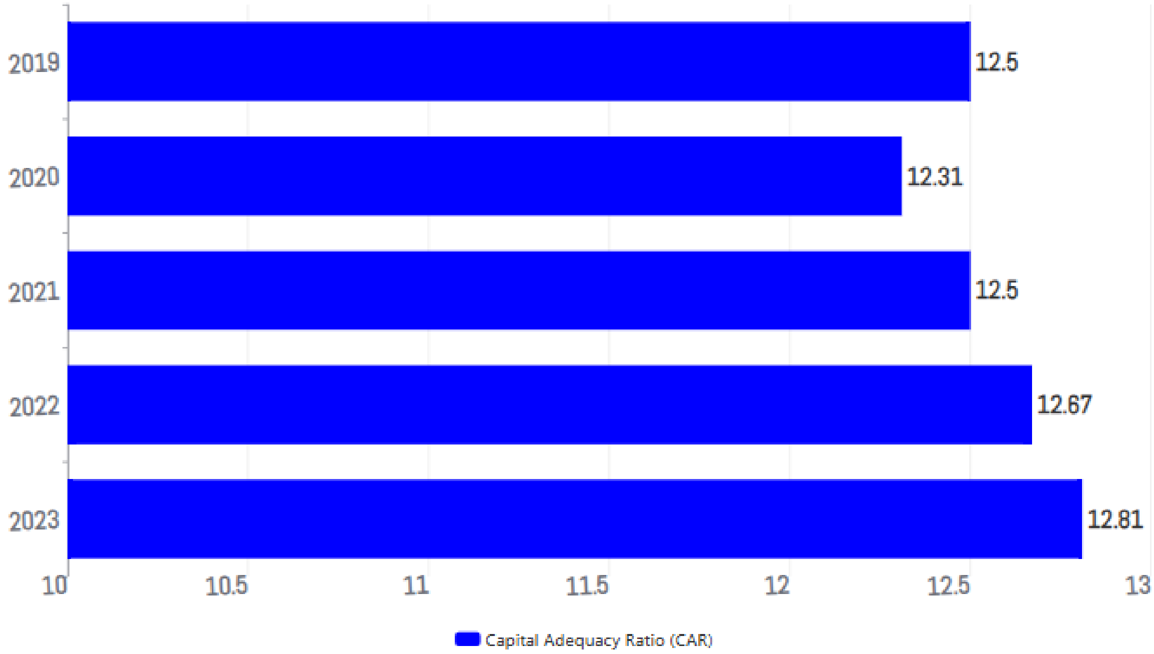
4.10: Capital Adequacy Ratio (CAR)

To evaluate the bank's ability to absorb potential losses and protect depositors, ensuring financial stability and compliance with regulatory standards.

Formula: $\text{CAR} = \left(\frac{\text{Tier 1 Capital} + \text{Tier 2 Capital}}{\text{Risk-Weighted Assets}} \right) \times 100$

Table-1.10: Capital Adequacy Ratio (CAR) from year 2019-2023

Years	2019	2020	2021	2022	2023
CAR (%)	12.50	12.31	12.50	12.67	12.81



Interpretation:

The Capital Adequacy Ratio (CAR) remained stable above the regulatory benchmark over the years, starting at 12.50% in 2019 and gradually improving to 12.81% in 2023. This reflects the bank's consistent efforts to maintain adequate capital to cover potential risks, ensuring financial resilience and compliance with standards.

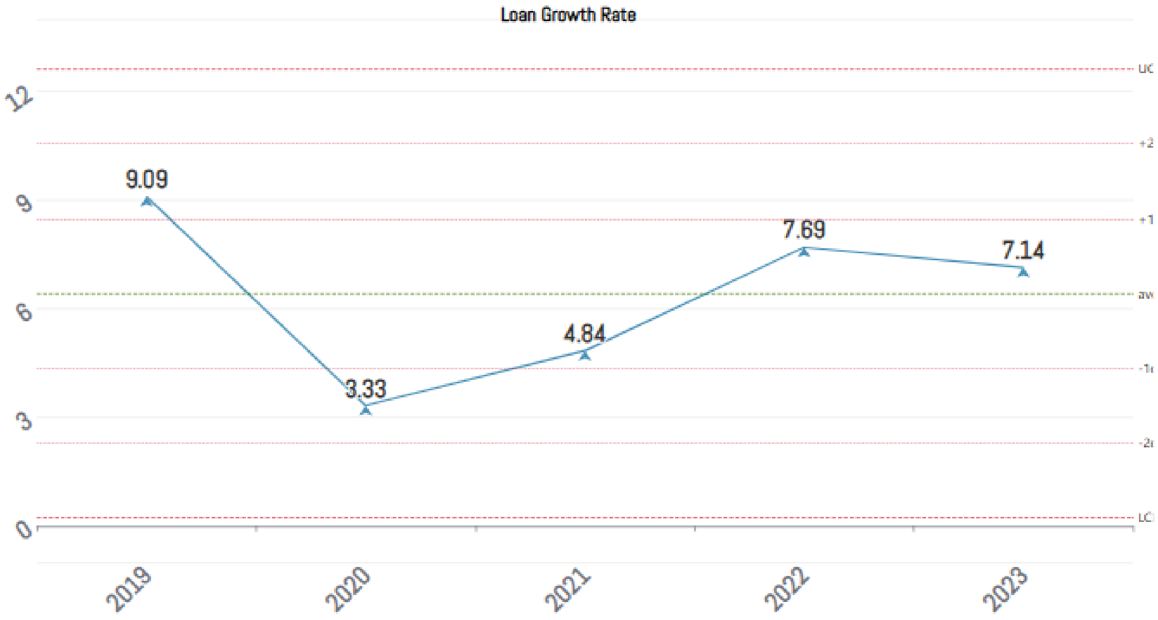
4.11: Loan Growth Rate

To assess the bank's loan portfolio growth, indicating how well the bank is expanding its lending activities over time.

Formula: $$\text{Loan Growth Rate} = \left(\frac{\text{Current Year's Loans} - \text{Previous Year's Loans}}{\text{Previous Year's Loans}} \right) \times 100$$

Table-1.11: Loan Growth Rate from year 2019-2023

Years	2019	2020	2021	2022	2023
Loan Growth Rate (%)	9.09	3.33	4.84	7.69	7.14



Interpretation:

The Loan Growth Rate exhibited strong growth in 2019, with a 9.09% increase from 2018 to 2019. From there, the growth rate slowed down, with 3.33% in 2020, followed by 4.84% in 2021. The growth picked up again in 2022 at 7.69%, before slightly decreasing to 7.14% in 2023. This indicates a steady but slightly decelerating pace of growth in the bank's loan portfolio over the years.

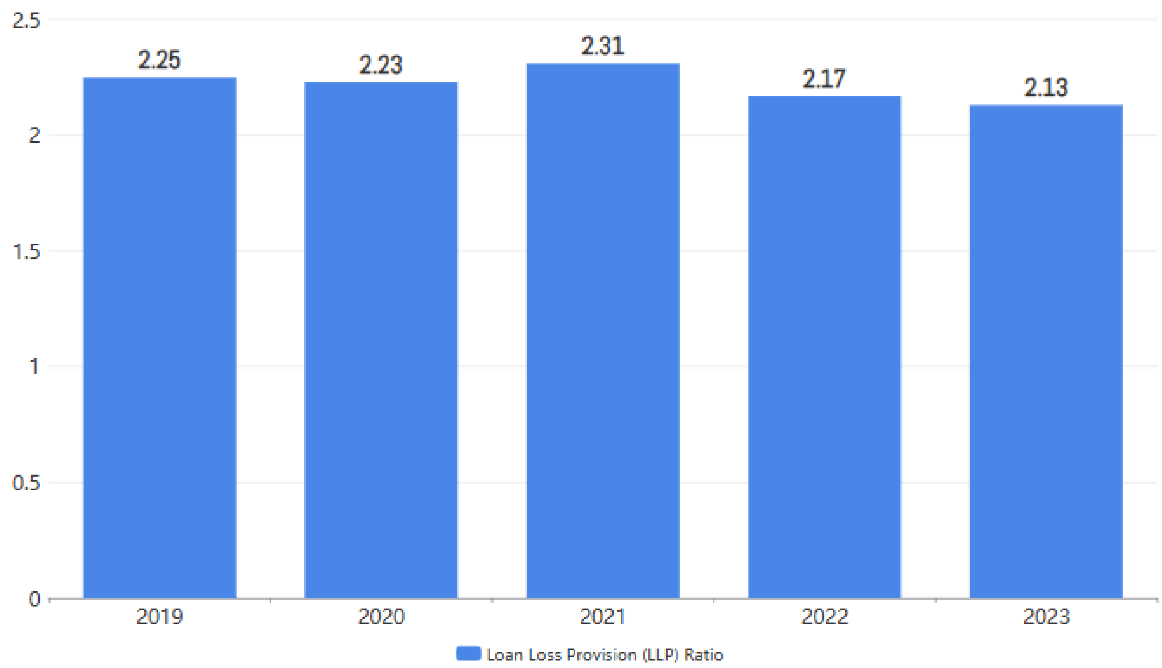
4.12: Loan Loss Provision (LLP) Ratio

To evaluate the bank's ability to cover potential loan losses by comparing provisions set aside for bad loans to the total loans, indicating the bank's risk management practices.

Formula: $$\text{LLP Ratio} = \left(\frac{\text{Provision for Loan Losses}}{\text{Total Loans}}\right) \times 100$$

Table-1.12: Loan Loss Provision (LLP) Ratio from year 2019-2023

Years	2019	2020	2021	2022	2023
LLP Ratio (%)	2.25	2.23	2.31	2.17	2.13



Interpretation:

The LLP Ratio remained relatively stable over the five years, starting at 2.25% in 2019 and decreasing slightly to 2.13% by 2023. This steady provision relative to total loans indicates that the bank has been consistently managing its potential loan losses, although the ratio decreased slightly in recent years due to growth in loans and more effective risk mitigation.

Chapter-5

Findings, Recommendations, and Conclusion

5.1: Findings

1. **Classified Loans**: The amount of classified loans increased from BDT 5,200 million in 2019 to BDT 6,000 million in 2021, before slightly decreasing to BDT 5,800 million in 2023. The consistent high levels of classified loans indicate ongoing credit quality concerns.
2. **Provision for Unclassified Loans**: Provision for unclassified loans increased from BDT 150 million in 2019 to BDT 210 million in 2023. This steady rise reflects growing concerns over unclassified loan risks, highlighting potential weaknesses in managing non-performing assets.
3. **Provision for Classified Loans**: Provision for classified loans grew from BDT 1,150 million in 2019 to BDT 1,400 million in 2023. Despite some fluctuation, the increasing provisions indicate rising risks and the need for the bank to strengthen its coverage for non-performing loans.
4. **Provision for Contingent Liabilities**: Provision for contingent liabilities increased from BDT 75 million in 2019 to BDT 95 million in 2023, indicating rising risks related to contingent liabilities and a need for better risk mitigation strategies.
5. **Non-Performing Loan (NPL) Ratio**: The NPL ratio rose from 8.67% in 2019 to a peak of 9.23% in 2021, reflecting increased non-performing loans. Although it decreased to 7.73**%** in 2023, the NPL ratio remains a concern for the bank's credit quality.
6. **Credit to Deposit Ratio (CDR)**: The CDR remained relatively stable, but it fluctuated from 75.00% in 2019 to 72.22% in 2021, and returned to 75.00% in 2023. The stable yet high CDR points to the bank's potential overreliance on deposits for lending, indicating a possible liquidity issue.
7. **Return on Assets (ROA)**: The ROA decreased from 0.80% in 2019 to 0.69% in 2020. However, it improved to 0.84% in 2023, showing a recovery, but the lower initial ROA indicates that profitability has been somewhat weak over the years.
8. **Return on Equity (ROE)**: The ROE dropped from 12.00% in 2019 to 10.00% in 2020. It recovered slightly to 11.43% in 2023, but the decline over the years indicates that the bank faced challenges in generating returns from its equity.
9. **Debt to Equity Ratio**: The debt-to-equity ratio increased from 9.00 in 2019 to 9.29 in 2023. This upward trend shows that the bank increasingly relied on debt financing, raising concerns about its financial leverage and risk exposure.

10. **Capital Adequacy Ratio (CAR)**: The CAR remained above the regulatory requirement but showed a marginal increase from 12.50% in 2019 to 12.81% in 2023. While compliant, the slight upward trend suggests the bank may still need to build stronger capital buffers to absorb risks.
11. **Loan Growth Rate**: The loan growth rate decreased significantly from 9.09% in 2019 to 3.33% in 2020, and remained lower than expected in 2021 (4.84%) and 2023 (7.14%). This slowdown in loan growth highlights a deceleration in the bank's lending activities.
12. **Loan Loss Provision (LLP) Ratio**: The LLP ratio decreased slightly from 2.25% in 2019 to 2.13% in 2023. While the ratio remained stable, the slight decrease suggests the bank may not be provisioning adequately for potential loan losses in comparison to loan growth.

5.2: Recommendations

1. **Classified Loans**: Implement stricter credit screening and improve collection efforts to reduce classified loans. The current classified loan level of BDT 5,800 million (2023) should be targeted for reduction by 10-15% in the next two years to improve loan quality.
2. **Provision for Unclassified Loans**: Increase provisions for unclassified loans, especially considering the growth from BDT 150 million in 2019 to BDT 210 million in 2023. A 10% increase annually could help cushion potential risks.
3. **Provision for Classified Loans:** Strengthen provisions for classified loans, which increased from BDT 1,150 million to BDT 1,400 million over five years. Increasing provisions by 15-20% annually can help ensure better risk coverage.
4. **Provision for Contingent Liabilities**: Increase provisions for contingent liabilities, which grew from BDT 75 million to BDT 95 million over five years. A 10-12% increase per year could enhance the bank’s risk mitigation for future obligations.
5. **Non-Performing Loan (NPL) Ratio**: The NPL ratio decreased from 9.23% in 2021 to 7.73% in 2023, but it is still high. The target should be to reduce this to below 5% in the next three years through improved loan monitoring and recovery efforts.

6. **Credit to Deposit Ratio (CDR)**: The CDR fluctuated but remained around 75.00%. The bank should target a 70-75% range to balance loan growth and liquidity, ensuring it does not overextend its lending capacity compared to deposits.
7. **Return on Assets (ROA)**: With the ROA at 0.84% in 2023, the bank should aim to increase it by 0.15-0.2% annually to improve profitability, through better asset utilization and cost management.
8. **Return on Equity (ROE)**: The ROE decreased from 12.00% to 11.43% over the years. Target a 2-3% increase in ROE annually to improve shareholder returns, focusing on profit growth and cost management.
9. **Debt to Equity Ratio**: The ratio increased from 9.00 to 9.29, indicating higher reliance on debt. Target a stable ratio below 9.0 by reducing debt and increasing equity in the next 2-3 years.
10. **Capital Adequacy Ratio (CAR)**: While the CAR is above the regulatory requirement, it should be increased by 0.5% annually to maintain a strong capital buffer, aiming for 13% or more to absorb future shocks.
11. **Loan Growth Rate**: Loan growth slowed to 7.14% in 2023. The target should be to increase this rate to at least 10-12% annually, focusing on expanding the loan portfolio and offering competitive products.
12. **Loan Loss Provision (LLP) Ratio**: The LLP ratio decreased slightly from 2.25% to 2.13%. A 1-2% increase in provisions can ensure the bank maintains adequate coverage against potential loan losses as its loan portfolio expands.

5.3: Conclusion

In conclusion, Al-Arafah Islami Bank PLC has shown steady growth in its credit operations from 2019 to 2023, though challenges remain, particularly with managing classified loans and maintaining a high NPL ratio. The bank has taken a proactive approach by increasing provisions for both unclassified and classified loans, as well as for contingent liabilities, which is a positive sign of its risk mitigation efforts. Despite fluctuations in credit and deposit ratios, the bank has maintained a stable capital adequacy ratio, indicating solid financial stability.

However, there are areas that require attention, such as improving the quality of the loan portfolio and maintaining better profitability ratios, as seen with the slight decline in ROA and ROE. The provision levels, although rising, should be closely monitored to ensure they remain sufficient to cover potential future risks, especially considering the increasing trend in classified loans.

The bank's performance in terms of loan growth and debt management demonstrates steady progress, but there is room for improvement, particularly in balancing the growth of assets with prudent risk management. With targeted strategies aimed at improving asset quality, reducing classified loans, and enhancing profitability, Al-Arafah Islami Bank can continue its upward trajectory while ensuring long-term financial health and stability.

Overall, while the bank has made commendable strides, the recommendations provided in the report can help address the existing challenges and further enhance the performance of Al-Arafah Islami Bank PLC in the coming years.

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