

DIRECTORS' REPORT TO THE SHAREHOLDERS



It gives me great pleasure to present on behalf of the Board of Directors 60th annual report of the bank for the year ended December 31, 2009. In November 2009, the Bank completed its 60th year of service to the country. On this auspicious occasion I give my heartiest facilitations to all the stake holders in NBP.

In the year 2009, the economy showed signs of stabilization. Inflation remains the top concern which eased to 10.7% by August, it's lowest in 20 months, as a result of monetary tightening. The current account deficit improved and foreign exchange reserves stabilized - mainly on account of lower oil prices and record remittances from workers abroad. Growth slid to 2% in 2008-09, scarcely outpacing population growth.

Problems in the energy sector, with demand outstripping generating capacity, depressed growth potential are key

burdens on public finances. Year 2009 witnessed unprecedented challenges; terrorism remained the biggest challenge for Pakistan and still is. The negative effects of international economic meltdown which started in 2008 were evident in 2009, with the sharp rise in non performing loans and rising cost of operations; these factors hampered the business confidence and performance of the banking sector.

EARNINGS PER SHARE INCREASED BY 18% TO RS.16.92 IN 2009. THE TOP LINE (OPERATING REVENUE) INCREASED BY 7.5% FROM RS. 53.4 BILLION IN 2008 TO RS. 57.5 BILLION IN 2009.

DIRECTORS' REPORT TO THE SHAREHOLDERS



In this backdrop it is commendable to note that NBP's after tax profit increased by 18% from Rs. 15.5 billion to Rs.18.2 billion. The said increase is owing to higher fee & commission income, tax credit and capital gains. Earnings per share increased by 18% to Rs.16.92 in 2009. The top line (operating revenue) increased by 7.5% from Rs. 53.4 billion in 2008 to Rs. 57.5 billion in 2009. Pre-tax profit however, has reduced to Rs. 22.3 billion, a decrease of 3% over last year mainly on account of higher administrative cost and provision charge which increased due to both fresh accretions and further downgrading of non performing portfolio. The bank has prudently provided for the non performing loans which is evident from the provision coverage ratio of 76 %, higher than the industry average.

Pre- tax return on equity stood at 27%, pre-tax return on assets at 2.6% while cost to income ratio is at 0.39. The bank is well capitalized with capital adequacy ratio at 16.9%.

Net interest income increased by 3.8 % or Rs. 1.4 billion from the corresponding period last year owing mainly to volume growth. The interest rates that were at record level in beginning of the year gradually decreased during the year. Cost of deposits increased mainly owing to the minimum rate of 5.0% for all remunerative deposits. The bank increased its deposits to strengthen liquidity position which though increased cost of fund, but its overall impact on the system's stability and liquidity outweighs the rise in cost.

Non-interest income shows growth of 16 % mainly due to increase in fee, commission and capital gains whereas the exchange income, dividend income as well as other income shows decline. Fee income increased by 13%, increase have been noted in commission on trade finance, general banking, arrangement & advisory services as well as government transactions. Income from dealing in foreign currencies decreased mainly on account of lower revaluation gains due to less volatility in Pak Rupee in the year under review. Other income is lower by Rs.693 million due to one off receipt of Rs.988 million compensation on delayed refunds last year. Dividend income decreased by Rs.959 million this year mainly on account of lower dividend declared on NIT units this year.

Capital gains show a sharp increase of Rs.4.2 billion over last year mainly on account of Rs. 3.9 billion gain on redemption of NIT Units. Salaries & Allowances increased as a result of annual increase in salaries, promotions and head count. Charges to defined plan shows sharp increase

due to additional charge of Rs.1.4 billion on account of revision in pension factor. Other administrative expenses increased mainly due to inflation, and branches up-gradation.

Provision charge against advances, investments & other assets increased by Rs. 572 million from Rs. 11.7 billion in 2008 to Rs.12.3 billion in 2009. The increase in provision charge is both due to fresh accretions as well as further downgrading of the portfolio. The increase in NPLs is an industry wide phenomena which increased by 25% in 2009. High inflation and interest rates, power shortages, pressure on trade volumes coupled with deteriorating law & order situation as a result of ongoing war on terror were the factors which seriously dampened the business confidence and as a result the repayment capacity of the borrowers was seriously affected which resulted in higher NPLs. Provision against investment is mainly on account of impairment loss recorded on equity portfolio.

Despite many challenges, NBP recorded an impressive growth both in terms of advances as well as deposits. By year end, the deposits increased by 16% or Rs.102 billion. The increase was in all categories of deposit. In case of advances the growth was mainly in commodity and corporate sector on account of higher borrowings by Government from commercial banks.

DIRECTORS' REPORT TO THE SHAREHOLDERS

Performance of the various business and support units during the year 2009 is given below:

Corporate & Investment Banking

Corporate & Investment Banking Group enjoys robust relationship with premier corporate clients. The length and breadth of our corporate clientele has been built on corporate strategy of providing comprehensive and customized financial solutions to our corporate customers. Varied banking and investment products are offered to the corporate clients from working capital financing to infrastructure project, structured and syndicated financing, divestitures, financial restructuring, mergers and acquisitions assignments and associated financing solutions. The group facilitated 122 projects and syndicate financing proposals which were mainly in financing for energy and power sectors. Advisory fee on corporate finance was a major contributor as the bank executed a number of large transactions in the energy and infrastructure projects. The bank also focused on increasing trade finance income by leveraging the bank's relationship with clients.

Corporate & Investment Banking Group is geared to take advantage of tremendous growth potential of corporate accounts and continued its efforts to remain a major contributor to the bank's earnings. It is striving to market new clients and retain the existing relationships and build market share through offering superior services, competitive pricing and wide product range to valued corporate clients.

Commercial & Retail Banking

NBP has the largest retail client base in the country with one of the highest retail portfolios. The bank's retail strategy focuses on its extensive branch network and leveraging the customer base. In 2009 however due to the high interest rate environment and pressure due to non performing loans, the consumer advances registered decline.

Despite an ailing economy and adverse macroeconomic factors, the Commercial & Retail Banking Group (C&RBG) closed 2009 with the key performance indicators being positive. The absolute domestic deposits base increased by 22% with emphasis on growth in low cost deposits. As a major initiative in this direction the bank launched CASA Deposit Mobilization Scheme in late 2009 aimed at mobilizing Current / Saving Accounts through incentivizing employees. With the increase in NPLs, the focus on recoveries has been heightened, along with prudent growth in advances.

SME financing is an area of good future potential. Due to negative impact of high inflation & interest rates, power shortages, fluctuation in commodity prices and reduction in export orders, this sector suffered considerable pressure that reduced the repayment capacity of the borrowers for existing loans and also their willingness to go for fresh financing. Due to these factors SME loans registered decline.

Commodity support prices were raised by the Government to provide much needed support and encouragement to the growers and as a result the loans under commodity operations witnessed robust growth during 2009 and increased by 110%. These loans are fully backed by GOP guarantee.



DIRECTORS' REPORT TO THE SHAREHOLDERS

Overseas Banking

National Bank of Pakistan is present in all major financial centers of the world; in Europe, USA, Hong Kong, Japan as well as in the emerging markets of Central Asia, South Asia and Far East to capture trade related business. Bank's overseas network is spread in 16 countries of the world comprising of 22 branches, a wholly owned subsidiary and a Joint Venture Bank in the United Kingdom besides three Representative Offices.



NBP overseas branches provide all kinds of banking facilities like accepting deposits, advances to individuals and corporate clients, participation in syndications and trade financing. The opening of Saudi Arabia branch is underway. In addition efforts are underway to upgrade Bank's existing Representative Offices in Tashkent and Beijing.

Agriculture Finance

The bank aims to cater to the entire farming and non-farming agriculture business and provides finances ranging from short to long term for the production and development of crops and non-crop items for agriculture business related to packing, grading, processing, storage, marketing and exports.

Pakistan's rural economy has high growth potential and offers attractive opportunities. The bank's product and services are offered to address the needs of both the farm and non farm sectors. NBP's large rural coverage of the country is second to none and is one of the major strengths of the bank. Presently, the agriculture financing facility is offered under the product category of NBP Kisaan Dost where 30 agriculture financing schemes are offered.

The importance of agriculture financing cannot be over emphasized as agriculture is key to Pakistan's future. Rural banking in Pakistan is in nascent stages and deployment of technology and modern banking channels continue to be an evolving process.

Treasury Management

NBP has the largest treasury in terms of size. Its function includes liquidity, exchange and interest rate management. The Bank is a major player in the foreign exchange and money market and is a primary dealer of government securities. It has the capability to offer structured products to its customers, including derivatives. For the banking industry, the year was very volatile in terms of interest rates, varying liquidity conditions, global credit tightening, depreciation of Pak Rupee and high inflation resulting in significant movements in yield curve. Treasury Management Group actively managed its portfolio and optimized yields.



DIRECTORS' REPORT TO THE SHAREHOLDERS

Islamic Banking

The bank believes that Islamic Banking offers good potential for growth. The bank has opened eight (8) branches since 2007, of which three were opened in 2009. During the last two years its asset size has grown significantly with offering of market-driven products like Murabaha and Ijarah. Islamic Banking is making its mark by catering to the Bank's already existing large customer-base as well as exploring new and untapped markets including SME, Commercial and Corporate. Islamic Banking is developing policies for new products like Diminishing Musharikhah, Salam and Istisna to meet customer's needs. The overall operations showed loss as a result of higher start up cost of three new branches opened this year.



Global Home Remittances Management

The Bank channelizes the remittance business through extensive overseas branch network. The Bank signed an agreement with Western Union for further increase in remittances business. The bank has also agreements in this regard with exchange companies in U.S., Europe, Central Asia, Middle East and Asia. Over the years, NBP has taken various measures to facilitate overseas Pakistanis to send their remittances through its branches.

Global Home Remittances Management Group was established with renewed focus to increase home remittances. With recent introduction of NBP e-Remittances, prompt and efficient transfer of credit to the beneficiary is ensured. The Group generated more than 50% growth in home remittances volume and transaction compared to last year marking a historical milestone for NBP and at the same time serving the country.

The bank also launched an effective marketing campaign in Pakistan and in the overseas market to promote NBP as 'choice for home remittances'. We have improved our service quality by developing effective complaint handling system in Pakistan.

Equity Investment Division

Equity Investments Division (EID) was formed in November 2009. Earlier Equity Investment was functioning under the umbrella of Corporate and Investment Banking Group. The main objective of EID is to build and maintain equity investment portfolio for NBP that provides attractive returns in terms of dividend income as well as capital gains.

EID is planning to diversify its investments by actively participating in the primary as well as secondary markets. Furthermore, EID is also responsible for investments



DIRECTORS' REPORT TO THE SHAREHOLDERS

in mutual funds, secondary trading in Term Finance Certificate, underwriting for companies and evaluating investments/divestments of unlisted companies. EID has been instrumental in structuring the acquisition of National Fullerton Asset Management Limited (NAFA). The deal is in final stages.

The role of this division becomes more significant after redemption of NIT Units against which the bank has received prorata ordinary shares portfolio. Going forward the Bank will be a major player of the capital market with the focus to optimize return.

Operations

NBP is continuously transforming its image and customer perception as a modern bank through branch renovation and relocation to more convenient and accessible sites. The team at Operations Group commits itself to change the face of the Bank by way of improving its physical outlook, effective implementation of its systems & controls and the quality of service provided to its customers. Improving operational efficiency is getting more focus given the challenges being faced by the industry. With opening of customer facilitation centers for the collection of utility bills and making payments to pensioners, the bank expects to reduce its counter traffic at branches thereby focusing more on its customer's business needs. Customer care is a key area of the bank and various training programs have been conducted for employees to improve customer handling and interaction.

Operations group has formulated and implemented various policies to improve efficiency and transparency in execution of banking operations. Special emphasis have been placed on development of Anti money laundering (AML) & Know your customer (KYC) policies.



Special Assets Management

Special Assets Management Group is primarily responsible for monitoring and settlement of non performing loans (NPLs) portfolio. With NPL coverage of more than 76% we believe that non performing loans can contribute substantially in the bank's profitability through recoveries and settlements.

Rising non-performing loans has been an industry wide phenomenon and due to adverse economic factors, NPLs increased by 26% or Rs. 14.5 billion. We believe that most of the NPLs are the result of business cycle / circumstantial defaults and with the economy picking up and reduction in interest rates; the quantum of non-performing loans is expected to decline. We are keeping our staunch focus on recovery and reduction in non performing loans is the area of greatest attention.



DIRECTORS' REPORT TO THE SHAREHOLDERS

Information Technology

National Bank of Pakistan is embarking on industry leading IT initiatives to upgrade and implement new application solutions to meet the challenges of growing competition and enhanced business requirements. Core Banking Application (CBA) contract has been signed with M/s Fidelity Information Systems and its implementation has started and by the end of 2010 three pilot branches are expected to come on this new IT platform. 250 more branches will be converted and the remaining branches shall come on the new platform in next three to four years. This will be a transformational change which will greatly improve operational efficiency and control, customer service and facilitate launch of new banking products. The existing legacy applications have been enhanced and upgraded. Five new capacity building projects were initiated i.e. Online Connectivity, Bandwidth Enhancement for core WAN links, Call Centre, ATMs Expansion, E-Channel Manager/CMS projects. The purpose of these initiatives is business integration and transition towards modern banking with a focus on customer facilitation.

Human Resource Management

The bank truly values its staff and the vital role they play in successful organizations. The bank gives special attention to attracting, developing and retaining good quality human resource. Our new hiring of top class MBAs as Management Trainees Officers (MTOs) and search for talent within the Bank have helped in preparing second and third tier leadership lines. 'Female Empowerment' was launched to empower female employees and impact communities by championing the cause of women's empowerment in the society. Today, NBP is determined in pursuing the policy of placing females on responsible and challenging position as Branch Managers, Branch Operations Managers and Customer Facilitation Officers. A number of female MTOs have been selected, trained and posted as branch managers. Currently, 60 branches are being headed by females. HR initiatives and strategy is amid at competitive employee compensation, training need assessment and succession planning. NBP is striving to become an employer of choice through improved HR policies and competitive remuneration.



Audit & Inspection

Internal Auditing is an independent, objective assurance and consulting activity designed to add value and improve organizational operations. It helps the bank accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and



DIRECTORS' REPORT TO THE SHAREHOLDERS

governance processes. In order to restructure the Audit & inspection Group in line with international best practices a detailed strategic plan has been evolved wherein time-bound action plan was chalked out to implement four pronged strategy to bring about a quality change in the functioning of audit and to change its approach from traditional procedure-based audit to a more sophisticated Risk Based & Value Added Audit & Management Consultancy. To achieve these goals we are hiring qualified staff, arranging appropriate training programs, encouraging audit functionaries to acquire professional qualifications, re-engineering systems, policies and structure of internal audit in line with our objective of undertaking risk-based and value-added activities.

Credit and Risk Management

NBP is continuously upgrading its risk management process to identify, evaluate and manage risk. Our focus includes analysis, evaluation and management of all risks which include credit, liquidity, market, operational and reputation risks. The bank's risk management policies and procedures are subject to high degree of supervision and guidance to ensure that all risk categories are systematically identified, measured, analyzed and proactively managed.

We have deployed value at risk (VaR) framework for measurement and monitoring of market risk. Operational Risk Management Unit has been established that supplements Credit and Market risk units for comprehensive risk management. Our risk management in terms of adoption of Basel II guidelines is advancing smoothly where consultants have been appointed to assist the bank in developing a robust framework for managing risk.

We have our internal filtration systems and approval hierarchy to ensure that proper authority and responsibility is established whilst reducing the lead processing time of the credit application. The bank has proper monitoring system with Credit Administration Department (CAD) to further improve risk management function.

Compliance

Compliance is an independent function that identifies, assesses, advises, monitors and reports on the Bank's compliance risk, i.e. the risk of legal or regulatory sanctions, financial loss or loss to the reputation which the bank may suffer as a result of its failure to comply with applicable laws, regulations, and codes of conduct and standards of best practices. The bank has accelerated its efforts proactively to strengthen compliance culture in the bank. During 2009 we have revised Compliance Review Program (CRP) to incorporate relevant changes in rules, regulations and changing dynamics to help senior management in identifying and assessing risk. In view of development of Compliance Review Program, Exception Reporting Mechanism has improved and now senior management receives report of violations promptly. Immediate corrective measures are initiated to secure the bank's interest.

Domestic Branches Network

We expanded our operations in 2009 and 11 more branches across Pakistan were opened in 2009 taking the domestic branch network to 1265. NBP has a well defined strategy for branch expansion to enter the untapped markets and to strike a balance between its rural and urban coverage.



DIRECTORS' REPORT TO THE SHAREHOLDERS

Credit Rating

NBP enjoys the highest rating of 'AAA' in the industry assigned by M/s JCR-VIS Credit Rating Company. The ratings assigned to NBP are primarily driven by the bank's role in the national economy as an agent of the State Bank of Pakistan and as a bank to the Government of Pakistan. Additionally, ratings also derive strength from the bank's consistently high capitalization levels, and nationwide access that has enabled it to secure a cost effective and diversified deposit base.

Social Responsibility

NBP has been at the forefront of socioeconomic development in the country. It has over the years funded projects which best serve the economic objectives and social needs of the country. The bank has made tremendous contribution to the development of small and medium sized entrepreneurs and to self-employment schemes. The Bank fulfils its social responsibility through contribution towards various causes. The Bank have always been generously donating in cases of national disasters and times of difficulty being faced by the nation, whether it was the devastating earthquake, flood relief efforts or the issue of Internally displaced persons (IDPs) the bank and its employees have been at the forefront to help and support the nation.



NBP realizing its responsibility towards improving natural environment accepted the challenge of planting saplings in an area of 3,000 hectares where severe deforestation has occurred over the years in the districts of Umerkot, Tharparkar and Mirpurkhas. The bank was applauded for its contribution in setting " Guinness World Record" for planting maximum number of trees in a single day. The record was set on 15th July 2009 in an area of Keti Bundar under the president's Mass Afforestation Program for plantation of 400,000 mangrove tree seedlings.



DIRECTORS' REPORT TO THE SHAREHOLDERS

Profit & Loss Appropriation

The Profit for the year 2009 after carry over of accumulated profit of 2008 is proposed to be appropriated as follows: -

	Rupees in Million
Net Profit before taxation for year 2009	22,300
Taxation	
Current year	9,221
Prior year(s)	(4,133)
Deferred	(1,000)
	<u>4,088</u>
After Tax Profit	18,212
Profit Brought Forward	52,456
Transfer from surplus on revaluation of fixed assets	124
Profit available for appropriation	<u>70,792</u>
Transfer to Statutory Reserve (10% of after tax profit)	<u>1,821</u>
Issue of bonus shares	1,794
Cash dividend	5,830
	<u>9,445</u>
Profit carried forward	<u><u>61,347</u></u>

Future Outlook

NBP remains committed to the interest of all stake holders including its employees, owners, regulators and the Pakistani nation. We have well defined strategy on where and how we want to proceed in the years to come. With the implementation of new 'Core Banking Package', NBP will completely automate its functions which in turn will appreciably enhance work efficiency. We will continue to diversify our customer segments thereby increasing our product offering. Our commitment towards the employees' empowerment / development will continue as we believe that a motivated and well trained work force is necessary to ensure sustenance and growth. On the business side our main focus would be to reduce non-performing loans and increase deposits.

We remain committed to our Vision, Mission & core values and our strategy for the future includes recovery efforts and revival of non performing loans, deposit mobilization, consolidation of loans, expense management and tapping into untapped markets by increasing our network both domestically and internationally. Customer service will remain our main focus of operations management.

The Board places on record its condolences for the sad demise of our director Mr. Sikandar Hayat Jamali on 25th of July 2009. His professionalism and prudent guidance served for the utmost betterment of our Bank.

The Board also places on record its appreciation for the services of Mr. Ayub Khan Tarin who have been replaced on the board by Ms. Nazrat Bashir. The Board remains indebted to the guidance and the insight provided by Mr. Tarin while he was on the Board.

The Board welcomes the induction of Mrs. Haniya Shahid Naseem and Ms. Nazrat Bashir as our Board members. We are confident that their experience and professionalism would add value and esteem for our stakeholders.



DIRECTORS' REPORT TO THE SHAREHOLDERS

REVIEW OF BOARD OF DIRECTORS' COMMITTEES AT NBP

At NBP, the Board of Director's have an active role in providing their able guidance and support to the Bank's management. For this purpose a number of Board's committees have been constituted in the bank. These committees have well defined terms of reference and they meet at regular intervals to review and make decisions on matters of importance for their respective area of functioning. The following are the committees:

Name of the Committee	Number of Directors	Number of Meetings held in 2009	Chairman of the Committee
Audit Committee	3	28	Mr. Ibrar A. Mumtaz
HR Management Committee	4	23	Mr. Mian Kausar Hameed
I.T Committee	3	14	Mr. Tariq Kirmani
Board Risk Committee	3	13	Mr. M Ayub Khan Tarin
Agriculture Finance Committee	3	11	Mr. Ibrar A. Mumtaz
Islamic Banking & Subsidiaries Committee	3	13	Mr. Tariq Kirmani
Sports & Culture Committee	3	11	Mr. Mian Kausar Hameed

Audit Committee

This committee has the oversight monitoring / assurance responsibility mainly relating to the effectiveness of the Bank's internal audit function, integrity of the Bank's financial statements, system of internal control, safeguarding of Bank's assets and associated risks, compliance with the applicable legal and regulatory requirements, corporate governance and Bank's "Code of Conduct" and co-ordination with external auditors, making recommendations with respect to other matters relating to their independence, performance, appointment and remuneration and approval of provision of other than audit services. The major achievement of the committee includes conducting a Quality Assurance Review of the bank's internal audit function through independent consultants to align the internal audit function with international standards/best practices of corporate governance. The Committee ensured independence of the Internal Audit function and further strengthened it in line with the requirements of International Standards on Internal Auditing, Institute of Internal Auditors USA, regulators and best practices of corporate governance.

28 meetings were conducted during 2009 and discussed the matters towards fiduciary, advisory and assurance responsibilities entrusted by the Board of Directors. The Committee reviewed various matters during the year for improvement in the internal audit, financial reporting, corporate governance, internal controls, risk management, compliance with relevant laws and regulations, code of conduct and external audit etc.



DIRECTORS' REPORT TO THE SHAREHOLDERS

HR Management Committee

The committee is an advisory and assurance committee which assists the board in fulfilling its responsibilities relating to all HR policy matters. It reviews and formulates human resource policies and best practices for attraction, retention, succession, motivation, training and development policies to achieve corporate objectives. It also recommends to the board the compensation, annual increase, performance bonuses, and perquisites of the CEO, Chief Internal Auditor, Secretary to the Board, CFO and all positions reporting to the CEO. It suggests strategies for negotiations with training and educational institutions both nationally & internationally for collaborating in training activities. It is also responsible for improvements in training methodology and identifying areas relevant to the needs of the organization. During 2009 several decisions were taken for improvement in the areas of HR policies, planning, training & development, compensation & pension, institutional discipline, and other HR related areas.

The Committee also discussed and directed to establish state of the art training institute to impart cutting edge knowledge, modern managerial and leadership skills to the employees of the Bank and enable them to face the challenges of ever changing environment. The committee emphasized the automation of all HR functions.

I.T Committee

The Committee is responsible for identifying areas of the prospective automation, reviews and decides strategic technology implementation and provides guidance and approves selection of appropriate technology solution; software, hardware, infrastructure and outsourcing.

For the first time in the history of National Bank a comprehensive IT strategy for the Bank was designed which encompasses the phase-1 focusing on "Strategy for Systems Quality Assurance & Testing Strategy (Policy, Procedures, Methodology and Framework)." The phase-2 of the strategy will cover the entire bank wide transformation and full spectrum automation, systems and data center integration, depth and width of IT Service Portfolio, IT Operations, plus incorporating the IT Internal Control Framework supported by COBIT, ISO ISMS 27001 and ITIL.

The ITBC has reshaped the IT Group's Organogram (Organizational Chart) to modernize and harmonize the entire IT Group with global and local best practices with a futuristic view to take IT into the new millennium. The new organizational chart also supports Enterprise Core Banking Application (CBA) Projects and the existing Banking Systems /Applications /Platforms.

ITBC kept a proactive oversight of all 20 Core Banking related projects through monthly meetings. Provided policy level guidance on bank wide transformation of all 1265 branches and Head Office from physical layouts to workflows, and data quality. ITBC assigned the Chief Information Security Officer to undertake the revamping of the Information Security Policy to achieve harmonization with ISO Information Security Management Systems 27001 standard, State Bank of Pakistan's guidelines and the COBIT Framework. ITBC approved the updated policy "Information Security Policy" (IT Security Policy v1.1) during the year 2009. The ITBC approved the Governance, Risk and Compliance (GRC) Stream / Project.



DIRECTORS' REPORT TO THE SHAREHOLDERS

Board's Risk Committee (BRC)

BRC over sighted the risk related issues of the bank and took several decisions for implementation. The functional scope of the Risk Management Committee is to develop the risk management role by identifying the relevant/new risk management tools as per Basel guidelines and developing the road map for implementing Basel II framework as per SBP guidelines. It also works for Risk & Exposure Reporting by development of Basel II's economic capital management frame work. This committee also provides the reporting and research for Board of Directors. It also reviews the liquidity position, forecasting and projections and portfolio of the Bank. In 2009 the committee approved rating model for corporate & commercial borrowers.

Beside this the BRC discussed in detail and took decisions on various issues; role & responsibilities of Risk & Audit, Risk reports, Risk Management Policy, Development on SaS Project, Regulatory Requirement, Progress on Basel II implementation, HR requirement of RMD, IRAF grading, Sectoral Analysis, Industrial Ratings, and Status of CIF project. Various MIS reports such as Monthly Risk Bulletin, an overview of operational risk management, operational risk report based on fraud & forgery data & SBP penalties were the key highlights discussed in the BRC meetings during 2009.

Agriculture Finance Committee

Agriculture Finance Committee directed restructuring and reorganization of Agriculture Finance Group and approved TOR, vision & mission statement of the group, Livestock/Dairy Farm Financing policy and Agricultural Finance Policy Manual. Particular emphasis was given to disbursement of finance to improve the yield/out put of this sector while maintaining the healthy recovery ratio.

31 Islamic Banking & Subsidiaries Committee

This Committee provides strategic guidance and recommends initiatives for expansions, mergers & acquisitions. The strategic endeavors resulted in expansion in NBP Islamic banking branch network covering all major cities of the country. To evaluate the commercial viability, future profitability and growth of Islamic banking, the committee guided Islamic Banking Group to prepare business plan for the year-2010 and henceforth strategic plan 2011-2013.

Registering the potential of Assets Management companies in Pakistan, particularly those backed by banks, the committee directed management to look into the formation of bank's own assets management company. The committee also facilitated an agreement between NBP Exchange Company (a wholly owned subsidiary) and Western Union for home remittances.

Sports & Culture Committee

The functional scope of the Committee is to devise strategies to promote sports and cultural activities in the bank as well as in the country. During 2009 the Committee reviewed the progress of various activities undertaken by the Sports, Culture & CSR Division and also approved various incentive and cash award policies for sportspersons working for NBP. The Committee also finalized the fee structure and membership rules & regulations of NBP Sports Club.



DIRECTORS' REPORT TO THE SHAREHOLDERS

The Committee also reviewed the performance of the Bank's sports teams and provided guidance and support to enhance their performance. The Committee also approved NBP Award for Excellence in Literature and devised modalities for evaluation of books. The Award ceremony was held in February-2009. NBP Sports Club was inaugurated in 2008 and is now fully functional and offers state of the art facilities to its members including health club, swimming pool, indoor tennis, badminton, squash, table tennis and snooker.



Corporate and financial reporting framework (Code of Corporate Governance)

The Board is fully aware of its responsibilities established by the Code of Corporate Governance issued by the Securities & Exchange Commission of Pakistan (SECP). The Directors are pleased to give the following declarations/statements to comply with the requirements of the Code.

- (a) The financial statements (Balance Sheet, Profit & Loss Account, Statement of Comprehensive Income, Cash Flow Statement, Statement of Changes in Equity and notes forming part thereof), prepared by the management of the bank give the information in the manner so required and respectively give a true and fair view of the state of the bank's affairs as at December 31, 2009 and of the results of its operations, changes in equity and its cash flows for the year then ended.
- (b) Proper books of accounts have been maintained.
- (c) Appropriate accounting policies have been consistently applied in preparation of the financial statements except for changes resulting on initial application of standards, amendments or interpretations to existing standards. Accounting estimates are based on the reasonable and prudent judgment.
- (d) The International Financial Reporting Standards, as applicable in Pakistan have been followed in preparation of the financial statements and departure there from, if any has been adequately disclosed.



DIRECTORS' REPORT TO THE SHAREHOLDERS

- (e) The system of internal control is sound in design and has been effectively implemented and monitored throughout the year. The Board is responsible for establishing and maintaining the system of internal control in the bank and for its ongoing monitoring. However, such a system is designed to manage rather than eliminate the risk of failure to achieve objectives, and provide reasonable but not absolute assurance against material misstatements or loss.

The process used by the Board to review the efficiency and effectiveness of the system of internal control includes, the following:

- The Board has formed various committees comprising of non-executive directors.
- Internal audit department of the bank conducts the audit of all branches, regions and groups at Head Office level on ongoing basis to evaluate the efficiency and effectiveness of internal control system and proper follow up of irregularities and control weaknesses is carried out.
- The Board receives confirmations / representations from all group and regional heads on annual basis confirming effectiveness of the internal control system established and maintained by them within their function.

The principal features of the bank's control framework include:

- The bank has clearly defined organizational structure, which supports clear lines of communications and reporting relationships.
- There exists a properly defined financial and administrative power of various committees and key management personnel, which supports delegations of authority and accountability.
- The bank has effective budgeting system in place. Annual budget of the bank is approved by the Board and monthly comparisons of actual results with the budget are prepared and reviewed by the senior management.

The bank has a comprehensive framework of written policies and procedures on all major areas of operations such as Credit, Treasury Operations, Finance, Internal audit and Compliance approved by the Board.

- (f) There are no significant doubts about the bank's ability to continue as a going concern.
- (g) There has been no material departure from the best practices of the corporate governance as detailed in the listing regulations.
- (h) Key operating and financial data is available in the annual report.



DIRECTORS' REPORT TO THE SHAREHOLDERS

The number of board meeting held during the year was 8 and attended by the directors as follows:

Syed Ali Raza	President / Chairman	8
Mr. Muhammad Ayub Khan Tarin	Director	8
Mr. Sikandar Hayat Jamali	Director	4
Mr. Tariq Kirmani	Director	8
Mian Kausar Hameed	Director	8
Mr. Ibrar A. Mumtaz	Director	8
Mrs. Haniya Shahid Naseem	Director	6

(j) Value of investments of Employees' Pension Fund and Employees Provident Fund as at December 31, 2009 (un-audited) was as follows:

	Rupees in '000
Employees Pension Fund	19,781,585
Employees Provident Fund	8,448,101

Pattern of Share holding

The pattern of share holding as at December 31, 2009 is given in Annual Report.

Earning per share

After tax earning per share for the year 2009 is Rs. 16.92.

Appointment of Auditors

The Board of Directors on the recommendation of the Audit Committee has recommended M/s Anjum Asim Shahid Rahman & Co. Chartered Accountants & M/s M. Yousuf Adil Saleem & Co. Chartered Accountants as statutory auditors for the year ending December 31, 2010. Both the firms being eligible offer themselves for appointment.

Risk Management Framework

NBP Board of Directors and Senior Management are fully committed to strengthen the Risk Management structure and practices. Several initiatives taken and planned by the Bank, in this regard, reflect commitment of Senior Management & Board of Directors to upgrade the quality of Risk Management process such as formation of Board Risk Committee, Executive Risk Management Committee, Basel II Implementation Committee, strengthening of Risk Management Division, conducting of exercises like Basel II Gap Analysis, Hiring of consultant for Basel II advisory services, implementation of software / systems for Credit Risk, designing of Internal Rating system, Scorecards for Consumer Credits, Revision and continuous improvement in policies, procedures, reporting structure for effective Risk Management and shift from fixed markup rate structure to floating rates for markup for managing Interest Rate Risk.



DIRECTORS' REPORT TO THE SHAREHOLDERS

Statement of Internal Controls

The Board is pleased to endorse the statement made by management relating to internal control. The Management's Statement on Internal Control is included in the Annual Report.

We extend our appreciation to the bank's staff for their commitment, dedication and hard work in achieving these excellent results. We would like to express our sincere reverence to the Board members whose valuable guidance has always enlightened us in our decision making. Finally we would like to express our appreciation to our stakeholders, regulators and our valued customers for their support and continued confidence in NBP.

On behalf of Board of Directors

S. Ali Raza

Chairman & President

Date: March 04, 2010



Statement of Internal Control

Reporting of Internal Control System

Bank Management has established and is managing an adequate and effective system of Internal Control which encompasses the policies, procedures processes and tasks as approved by the Board of Directors that facilitate effective and efficient operations. The management and the employees at all levels within the Bank are required to perform as per these approved Internal Control System components. The Internal Control System ensures quality of external and internal reporting, maintenance of proper records and processes, compliance with applicable laws and regulations, and internal policies with respect to conduct of business.

The management ensures that an efficient and effective Internal Control Systems is in place by identifying control objectives, reviewing existing procedures and policies and ensuring that control procedures and policies are amended from time to time wherever required.

However, Internal Control is designed to manage rather than eliminate the risk of failure to achieve objectives and provide reasonable but not absolute assurance against material misstatement or loss.

Evaluation of Internal Control

The Bank has an independent Internal Audit & Inspection function in the name of Audit & Inspection Group with three Audit Offices that conduct audit of branches, Regions and Group at Head Office on an on-going basis to evaluate the efficiency and effectiveness of Internal Control System. In addition to that Compliance set up is also in place with 145 independent Compliance Officers in Category III Branches and 28 Regional Compliance Chiefs and a regional compliance officer in Gilgit sub region with supporting staff to take care of Compliance related issues to strengthen the control environment.

For the year 2009 the Bank has made its best efforts to ensure that an effective internal control system continues to perform in letter and spirit. The observations made by the external / internal auditors and SBP inspection team in their respective audits/ inspections are promptly reviewed and measures are taken by the Board , Board Audit Committee and management for rectification of such observations to safeguard the Bank's interest.

We assess that the internal control environment is showing signs of improvement as compared to previous years in all areas of the bank. The bank is endeavoring to further refine its internal control design and assessment process as per guidelines issued by the State Bank of Pakistan. Accordingly, Bank is making all possible efforts to improve the professional skills and competency level of staff through need based training programs.

Imam Bakhsh Baloch
SEVP/ Group Chief
Audit & Inspection Group

Tariq Jamali
SEVP/ Group Chief
Compliance Group

Karachi
Date: March 4, 2010

Sha'riah Advisor's Report for the Financial Year 2009

For the year ended December 31, 2009

Alhamd-u-lillah with the grace of Allah Taa'la, I Abdul Sattar Laghari have reviewed/examined on test check basis, each class transaction, the relevant documentation and procedures adopted by Islamic Banking Branches/Group (IBBs & IBG NBP), and I hereby report that in my opinion;

- I) **The business and overall affairs** of IBBs carried out during the year 2009 are in accordance with Shariah principles and also these affairs are in compliance with SBP Shariah Guidelines. In random check & sampling and complete overview where deemed necessary, I highlighted any deviation and meticulous compliance thereto was ensured.
- II) In the financial year 2009 there were no major disbursements made by NBP, IBG. In order to check the **present outstanding portfolio** I audited and viewed transaction flows and conduct of account of the customers.
- III) Islamic PLS Account is a deposit facility which enables the customers to utilize their savings in an Islamic way and earn halal profits. **The profit and loss sharing scheme (PLS)** was launched in the beginning of this year and it was managed according to Shariah principles and the Shariah guidelines issued by the State Bank of Pakistan throughout the year.
- IV) Any **earnings** that have been realized from prohibited sources or by declaring the transaction void (Fasid) have not been pointed out with grace of Allah Taa'la.
- V) However IBG received an amount of three million rupees in **charity account**. This amount was distributed equally to the three approved charity organizations as per the policy of the charity.
- VI) **Training & Development of Human Resource** is an integral part for learning and growth of the employees. In order to inculcate basic understanding of Shariah Principles related to economics & finance and Asset & liability side of Islamic Banks, the staff members of IBBs ranging from Branch Managers, Operation Managers and other field functionaries were trained in basics of Islamic Banking and Finance by a sequence of comprehensive courses conducted by IBG at NBP Staff College, Islamabad & JNMDC, Karachi.

May Allah Taa'la bless us with best tawfeeq to accomplish these cherished tasks, make us successful in this world and in the hereafter, and forgive our mistakes.

Abdul Sattar Laghari
Sha'riah Advisor

Karachi
Date: March 4, 2010

8209

Statement of Compliance with Code of Corporate Governance

For the year ended December 31, 2009

This statement is being presented to comply with the Code of Corporate Governance (the Code) contained in the Regulation No: 36 & 37, XIII of listing Regulations of Karachi, Lahore & Islamabad Stock Exchange (Guarantee) Limited for the purpose of establishing a framework of good governance, whereby a listed Company is managed in compliance with the best practice of Corporate Governance.

The Bank has complied with the principles contained in the Code in the following manner.

1. The Board of Directors of the Bank is appointed by the Government of Pakistan (GoP) as per the provisions of the Banks' (Nationalized) Act 1974. At present all the Directors (except for the President/ Chief Executive who is also the Chairman of the Board) are independent non-executive Directors, including the Director representing minority shareholders as required by the Code.
2. The Directors have confirmed that none of them is serving as a Director in more than ten Listed Companies including the Bank.
3. All the Directors of the Bank are registered as Tax Payers and none of them has defaulted in payment of any loan to Banking Company, a DFI or an NBFI or being a member of Stock Exchange, has been declared as defaulter by the Stock Exchange.
4. During the year one of the directors Mr. Mohammad Arshad Chaudhry resigned w.e.f 14.02.2009 and another director Mr. Sikandar Hayat Jamali expired on 25th July, 2009. In terms of Section 11 (III-A) of Banks Nationalization Act, 1974, Federal Government appoints directors in consultation with SBP. Presently the appointment of directors in their place is under consideration with Ministry of Finance.
5. The Directors have confirmed that neither they nor their spouses are engaged in the Business of Stock Brokerage.
6. The Bank has prepared "Statement of Ethics and Business Practice" which is already approved by the Board of Directors.
7. The Board has approved the Vision, Mission, Core Values, Objective and NBP Strategic plan.
8. The Bank has comprehensive frame work of written policies and procedures on all major areas of Operations such as Credit, Treasury Operations, Finance, Internal Audit and Compliance etc. Many of these policies have been approved by the Board and are being constantly reviewed.
9. There exists in the Bank a frame work defining the limit of the authority of various Management levels. All the powers were exercised by the relevant authorities within the materiality thresholds.
10. All the Powers of the Board have been duly exercised and decisions on Material Transactions have been taken by the Board.
11. The meetings of Board of Directors were presided over by the Chairman. The Board met 8 times during the year. Written notices of the Board meetings, along with Agenda and working papers were circulated atleast seven days before the meetings. The minutes of the meetings were appropriately recorded.
12. The Bank held orientation course for the directors in the year, 2008. Further one director is attending training course at PICG.
13. The appointment of CFO, Company Secretary and Head of Internal Audit, including their remuneration and terms and conditions of employment are duly approved by the Board.
14. The Directors' Report for the year has been prepared in compliance with the Code of Corporate Governance and fully describes the salient matters enumerated in the Annual Report.
15. The Financial Statements of the Bank were duly endorsed by CEO and Financial Controller before approval of the Board.
16. The Directors, CEO and Executives have confirmed that they do not hold any interest in the shares of the Bank except as mentioned in the report.
17. The Bank has complied with all the Corporate and Financial Reporting requirements of the Code. In accordance with the requirement of clause (xiii a) of the listing regulations, all related party transactions have been reviewed and approved by the board of directors.
18. The Board has formed a Board Audit Committee comprising of three Non Executive Directors.
19. The Board Audit Committee held 28 meetings besides one full day orientation for the Directors as well as meeting held prior to the approval of Interim and Final Results as required by the Code. The Charter of the Board Audit Committee has been duly approved by the Board of Directors and has been advised to the Committee for compliance.

Statement of Compliance with Code of Corporate Governance

For the year ended December 31, 2009

20. The Board has setup an effective Internal Audit function. All the Branches, Regions, Staff Colleges, Subsidiaries and Groups are subject to Audit. All the Internal Audit Reports are accessible to the Board Audit Committee and important points arising out of audit are reviewed by the Board Audit Committee and important points requiring Board's attention are brought into their notice.
21. The Statutory Auditors of the Bank have confirmed that they have been given a satisfactory rating under the Quality Control Review Program (QCRP) of the Institute of Chartered Accountants of Pakistan, that they or any of partners of the firms, their spouses and minor children do not hold shares of the Bank and that the firms and all of their partners are in compliance with International Federation of Accountants (IFA) on Code of Ethics as adopted by the Institute of Chartered Accountants of Pakistan.
22. The Statutory Auditors or the persons associated with them have not been appointed to provide other services except in accordance with the Listing Regulations and the Auditors have confirmed that they have observed IFA guidelines in this regard.
23. We confirm that all other material principles contained in the code have been complied.

On behalf of the Board of Directors

S. ALI RAZA
Chairman & President

Karachi
Date: March 4, 2010

8209

Auditors' Review Report to the Members on Statement of Compliance With the Best Practices of Code of Corporate Governance

Anjum Asim Shahid Rahman & Co.
Chartered Accountants
1st & 3rd Floor, Modern Motors House
Beaumont Road
Karachi 75530, Pakistan

M. Yousuf Adil Saleem & Co.
Chartered Accountants
Cavish Court, A-35, Block 7 & 8
KCHSU, Shara-e-Faisal
Karachi 75350, Pakistan

We have reviewed the Statement of Compliance with the best practices (the Statement) contained in the Code of Corporate Governance (the Code) prepared by the Board of Directors of National Bank of Pakistan (the Bank) to comply with the Regulation G-1 of the Prudential Regulations for the Corporate / Commercial Banking issued by the State Bank of Pakistan, Listing Regulation No. 35 of the Karachi Stock Exchange, Chapter XI of the Lahore Stock Exchange and Chapter XI of the Islamabad Stock Exchange, where the Bank is listed.

The responsibility for compliance with the Code is that of the Board of Directors of the Bank. Our responsibility is to review, to the extent where such compliance can be objectively verified, whether the Statement reflects the status of the Bank's compliance with the provisions of the Code and report if it does not. A review is limited primarily to inquiries of the Bank's personnel and review of various documents prepared by the Bank to comply with the Code. The Statement of the Bank for the year ended December 31, 2008 was reviewed by Ford Rhodes Sidat Hyder & Co. Chartered Accountants and M. Yousuf Adil Saleem & Co. Chartered Accountants who through their report dated March 18, 2009 expressed an unmodified conclusion thereon.

As part of our audit of financial statements, we are required to obtain an understanding of the accounting and internal control systems sufficient to plan the audit and develop an effective audit approach. We are not required to consider whether the Board's statement on internal control covers all risks and controls, or to form an opinion on the effectiveness of such internal controls, the Bank's corporate governance procedures and risks.

Further, Listing Regulations of Karachi, Lahore and Islamabad Stock Exchanges require the Bank to place before the Board of Directors for their consideration and approval related party transactions distinguishing between transactions carried out on terms equivalent to those that prevail in arm's length transactions and transactions which are not executed at arm's length price recording proper justification for using such alternate pricing mechanism. Further, all such transactions are also required to be separately placed before the audit committee. We are only required and have ensured compliance of requirement to the extent of approval of related party transactions by the Board of Directors and placement of such transactions before the audit committee. We have not carried out any procedures to determine whether the related party transactions were undertaken at arm's length price or not.

Based on our review, nothing has come to our attention, which causes us to believe that the Statement does not appropriately reflect the Bank's compliance, in all material respects, with the best practices contained in the Code as applicable to the Bank, for the year ended December 31, 2009.

Anjum Asim Shahid Rahman & Co.
Chartered Accountants

M. Yousuf Adil Saleem & Co.
Chartered Accountants

Karachi
Date: March 4, 2010

Independent Auditors' Report To The Members

Anjum Asim Shahid Rahman & Co.

Chartered Accountants
1st & 3rd Floor, Modern Motors House
Beaumont Road
Karachi 75530, Pakistan

M. Yousuf Adil Saleem & Co.

Chartered Accountants
Cavish Court, A-35, Block 7 & 8
KCHSU, Shara-e-Faisal
Karachi 75350, Pakistan

We have audited the annexed balance sheet of **National Bank of Pakistan** (the Bank) as at December 31, 2009 and the related profit and loss account, statement of comprehensive income, cash flow statement and statement of changes in equity together with the notes forming part thereof (here-in-after referred to as the 'financial statements' for the year then ended, in which are incorporated the unaudited certified returns from the branches except for eighty branches which have been audited by us and twelve branches audited by auditors abroad and we state that we have obtained all the information and explanations which, to the best of our knowledge and belief, were necessary for the purposes of our audit.

It is the responsibility of the Bank's Board of Directors to establish and maintain a system of internal control, and prepare and present the financial statements in conformity with approved accounting standards and the requirements of the Banking Companies Ordinance, 1962 (LVII of 1962), and the Companies Ordinance, 1984 (XLVII of 1984). Our responsibility is to express an opinion on these statements based on our audit. The financial statements of the Bank for the year ended December 31, 2008 were audited by Ford Rhodes Sidat Hyder & Co., Chartered Accountants and M. Yousuf Adil Saleem & Co., Chartered Accountants who through their report dated March 18, 2009 expressed an unqualified opinion thereon.

We conducted our audit in accordance with the International Standards on Auditing as applicable in Pakistan. These standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of any material misstatement. An audit includes examining, on a test basis, evidence supporting amounts and disclosures in the financial statements. An audit also includes assessing the accounting policies and significant estimates made by management, as well as, evaluating the overall presentation of the financial statements. We believe that our audit provides a reasonable basis for our opinion and after due verification, which in case of loans and advances covered more than sixty percent of the total loans and advances of the Bank, we report that:

- (a) in our opinion proper books of account have been kept by the Bank as required by the Companies Ordinance, 1984 (XLVII of 1984), and the returns referred to above received from the branches have been found adequate for the purposes of our audit;
- (b) in our opinion:
 - (i) the balance sheet and profit and loss account together with the notes thereon have been drawn up in conformity with the Banking Companies Ordinance, 1962 (LVII of 1962), and the Companies Ordinance, 1984 (XLVII of 1984), and are in agreement with the books of account and are further in accordance with accounting policies consistently applied, except for the changes described in note 5.1 with which we concur;
 - (ii) the expenditure incurred during the year was for the purpose of the Bank's business; and
 - (iii) the business conducted, investments made and the expenditure incurred during the year were in accordance with the objects of the Bank and the transactions of the Bank which have come to our notice have been within the powers of the Bank;
- (c) in our opinion and to the best of our information and according to the explanations given to us the balance sheet, profit and loss account, statement of comprehensive income, cash flow statement and statement of changes in equity together with the notes forming part thereof conform with approved accounting standards as applicable in Pakistan, and give the information required by the Banking Companies Ordinance, 1962 (LVII of 1962), and the Companies Ordinance, 1984 (XLVII of 1984), in the manner so required and give a true and fair view of the state of the Bank's affairs as at December 31, 2009 and its true balance of the profit, its comprehensive income, its cash flows and changes in equity for the year then ended; and
- (d) in our opinion Zakat deductible at source under the Zakat and Ushr Ordinance, 1980 (XVIII of 1980), was deducted by the Bank and deposited in the Central Zakat Fund established under Section 7 of that Ordinance.

Anjum Asim Shahid Rahman & Co.
Chartered Accountants

Engagement Partner
Muhammad Shaukat Naseeb

Karachi
Date: March 4, 2010

M. Yousuf Adil Saleem & Co.
Chartered Accountants

Engagement Partner
Syed Asad Ali Shah

NBP SAIBAAN

HOME FINANCE



NBP Saibaan

- Home Purchase
- Home Construction
- Home Renovation
- Purchase of Land + Construction
- Balance Transfer Facility (BTF)



NBP

National Bank of Pakistan

The Nation's Bank

NBP CORPORATE BANKING



NBP Corporate Banking

NBP further consolidated its position as one of the top players in corporate and investment banking of the country in 2009 and has built a strong customer relationship with premier corporate clients.



NBP

National Bank of Pakistan

The Nation's Bank