



**RATINGS (DECEMBER 2010)**

**ESCORTS INVESTMENT BANK LIMITED (EIBL)**

	NEW
<b>ENTITY</b>	
Long Term	A-
Short Term	A2

**Financial Data (PKR in million)**

	30-Jun-10	30-Jun-09	30-Jun-08
Total Assets	1825	2108	6497
Equity	518	597	852
Net Income	-77	-166	138
ROE (%)	-14	-22	17
Debt/Equity %	235.7	234.3	634.7

**ANALYSTS**

Samiya Mukhtar  
+92 42 3586 9504  
samiya@pacra.com

Rana Muhammad Nadeem  
+92 42 3586 9504  
nadeem@pacra.com

**PROFILE:**

EIBL, incorporated in 1996, is listed on the Karachi and Lahore Stock Exchange and is majority owned (71%) by Bashir Family, directly by individuals and through a group company – ESSEM Power (Pvt.) Limited. Escorts group has interests in different sectors – Investment Banking, Brokerage, Electricity Meters manufacturing, and Hospitality industry. The main sponsor of the group is Mr. Bashir Ahmed – an electrical engineer by qualification. He is also the chairman of a seven member board. Ms. Shazia Bashir – elder daughter of Mr. Bashir – has been lately elevated (April 2010) to the position of the CEO of the bank. She has over fourteen years of professional experience in EIBL. She is ably supported by a mix of relatively young and experienced team of professionals.

**RATING RATIONALE AND KEY DRIVERS**

- The ratings reflect EIBL's relatively low risk profile characterized by its ability to largely absorb the impact of recent downturn in the economic environment in general, and non-banking financial sector in particular. However, limited business avenues has squeezed the bank's capacity to generate sufficient economic returns. Meanwhile, though the bank is low-leveraged, there exists a gap between the earning assets and related liabilities, thereby resulting in weak performance. Cognizant of the same, the management has taken various initiatives to explore the non-fund based avenues to achieve profitability while rationalizing existing cost structure. At the same time, the bank is making efforts to convert certain non-earning assets into economically viable resources. Nevertheless, extent and timely materialization of the bank's initiatives into sustainable revenue streams remains to be seen.
- The ratings are dependent on the bank's ability to successfully execute the new business strategy in order to strengthen its business and financial profile. Though the current credit exposure remain limited, the bank may need to further strengthen the existing risk management systems for future growth. Meanwhile, compliance with regulatory minimum capital requirement through either sponsor's support or with internal generation would remain critical for the ratings, going forward.

**ASSESSMENT**

- EIBL initially had been in commercial operations with three licenses – Investment Finance Services (IFS), Housing Finance, and Leasing. However, with changing market conditions and relatively stringent regulatory capital requirements in recent years, the bank prioritized IFS as its mandate for future growth and surrendered the other two licenses. Historically, bank's business model has remained tilted towards capital market activities with equity investments and placements or short term financing against shares as the primary earning assets and related income including capital gains, and dividends as major source of revenues while generating healthy profitability.
- Subsequent to 2008 stock market crises, EIBL's asset size squeezed significantly. In the absence of healthy capital market activities, interest income generated from relatively small loan book remained insufficient for the bank to cover its operating expenses and impairment losses. Moreover, the funds tied up in non revenue generating assets including relatively high fixed and other assets remained a drag on overall performance of the bank. Meanwhile, the brokerage operations, which are run through a wholly owned subsidiary – Escorts Capital Limited – could not produce any dividend stream for the bank in line with brokerage industry subdued trends, consequently, the bank incurred losses in last two years.
- Cognizant of these issues and other inherent constrains to NBFCs businesses, the management of the bank has embarked upon a new business strategy while addressing the need to rationalize cost structure and introduction of new products which are less dependent on capital market activities. Also, the bank is making efforts to convert key non earning assets into earning assets. In the recent past, the management has taken various initiatives to enhance and improve its fee based portfolio while restricting fund based asset expansion. These include interalia, plans to introduce home remittance services, REITs advisory, legal advisory, and mutual fund advisory and distribution services. The bank has attained some success in this regard. However, timely and successful conversion of these initiatives in adequate and sustainable revenue streams remains to be seen.
- Over the past few years the bank has been able to largely sustain its asset quality through close monitoring of existing loans and recovery of impaired portfolio. Meanwhile, the bank has already provided 90% of the impaired portfolio. Currently around 48% of the performing loan book is concentrated in loans to Escorts group companies. The bank expects its asset quality to strengthen further, going forward. The credit risk may increase in future as the bank plans to undertake margin financing business as soon as the financing product is approved by the regulator. Additionally, the management intends to have cautious expansion in its loan book. Keeping in view, further strengthening of risk management processes to minimize credit shocks would remain important.
- The bank follows an entity wide risk management process, and policies and procedures are well documented. The bank has currently outsourced its internal audit department to a well recognized audit firm. However, due to relatively small size of the bank, the segregation of duties in terms of business origination and oversight of related risks appears to be limited which may hinder bank's performance in case the growth opportunities materialize.
- Bank's investment portfolio mainly comprises Pakistan investment Bonds (71%), which are relatively more exposed to interest rate and price risk, though liquid. However, bank's asset liability matching remains weak. Nevertheless, un-utilized credit lines provide comfort in managing any foreseeable mismatches.
- Funding sources remain a mix of CoIs (32%), and Borrowing from financial institutions (67%), with the latter regardless of type of borrowing, being a key source of funding. Borrowing from financial institutions include an outstanding TFC of PKR 248 mln at end Sep-10. The CoIs are mainly mobilized from individuals (91%), while the concentration of top twenty remains very high (72%). The capital structure remains relatively less leveraged. However, business losses in last two years have eroded a major portion of the equity thereby weakening the risk absorption capacity of the bank and making difficult for it to meet the minimum capital requirements set by the regulator. Sponsors are committed to support the bank if the need arises. However, timely demonstration of the same and ability of the bank to generate required profitability to meet these requirements and revive its business profile would remain critical, going forward.