

## IGI FINEX SECURITIES LIMITED (IFSL)

### RATINGS (JANUARY 2010)

#### IGI FINEX SECURITIES LIMITED (IFSL)

Entity	New	Previous
Long Term	A-	A-
Short Term	A1	A1

### FINANCIAL DATA

#### PKR (mln)

	FY09	FY08	FY07
Total Assets	724	2,129	1,589
Equity	318	522	527
Brokerage Revenue	77	153	96
Net Income	(205)	26	27
ROE (%)	-48.8	4.9	9.7
ROA (%)	-14.3	1.4	2.8

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### RATING RATIONALE AND KEY DRIVERS

- The ratings of IFSL reflect its association with Packages Group – a leading business conglomerate of Pakistan. Furthermore, minimal market risk emanating from the policy against maintaining a proprietary equity trading book lends support to the ratings. However, the ratings take into account the suppressed socio-economic environment in Pakistan, which has pressurized stock markets' performance and resultantly lowered brokerage volumes. Moreover, significant losses, mainly on account of customer defaults, has impacted the company's risk absorption capacity.
- The ratings are dependent upon IFSL's ability to capitalize on its group's strengths to develop a strong and sustainable market share besides improvement in overall industry prospects. At the same time, strengthening of risk management procedures and control mechanism would be important. Meanwhile, any prolonged downturn in stock market volumes leading to a decline in brokerage business is likely to have negative implications for the ratings.

### ASSESSMENT

- The substantial deterioration witnessed in the socio-economic fundamentals of Pakistan, alongwith the global financial meltdown, in the recent period has impacted the stock market's performance, and in turn lowered brokerage volumes. The stock market, which experienced remarkable growth over the past few years, had a turbulent FY09, characterized by unprecedented 3-month long floor mechanism on trading and crash of stock prices, though this has experienced certain recovery later on. However, this crisis, while weakening a number of equity broking houses, has highlighted the requisite traits. The market players, having stable alternative sources of revenue, flexible cost structure, proactive management, and sound risk management system, were better able to withstand the difficult environment.
- In line with the market dynamics, IFSL's brokerage revenues declined sharply (~50%) in FY09. However, mark-up from bank deposits and placements, despite being modest supported its operating income. Although IFSL managed to control its operating expenses, a significant rise in provisioning against doubtful debts (FY09: 147mln, FY08: Nil) turned the bottom-line into red. During 1Q10, IFSL's brokerage revenue has shown growth and is expected to recover further with gradually improving interest in the stock market. Going forward, it would be crucial for ISFL to improve its market share (FY09: ~5%) while strengthening its ability to withstand adverse business environment through effective management and controls.
- IFSL's management envisages increasing its market share by penetrating further into the retail segment, which currently contributes around one-fourth of its total brokerage revenues. It plans to achieve this through advancements in 'I-Trade', IFSL's online trading platform. Currently, over 2,000 customers, constituting around half of the total investor base of IFSL use this platform.
- During the period leading up to imposition of floor mechanism on trading, IFSL, like most market participants, was actively engaged in Continuous Funding System (CFS) financing. Once trading ceased, a few trade debtors refused to honour margin calls and IFSL was unable to square their positions in the open market. Upon lifting of floor in Dec-08, the stock prices declined sharply, limiting IFSL's ability to cover its losses entirely by selling the securities. Although a major portion of the bad debts was later recovered, recoveries of over PKR 150mln remained in default. Nonetheless, IFSL prudently provided for almost the entire amount (PKR 147mln) during FY09.
- The recent crisis in stock market has magnified the significance of credit risk management. Accordingly, IFSL's management intends to increase its focus on developing a sound risk management function. At the same time, regulator's initiatives to discourage risk prone market financing products would further assist in mitigating credit risk. Currently, IFSL is largely transacting against cash only, barring for a few reputable institutions and high net-worth individuals, who are being facilitated through delivery versus payment (DVP) mechanism. However, effective implementation of risk management framework to counter both operational and credit risks would remain a major challenge.
- The board of IFSL has restricted its management from maintaining a proprietary equity trading book to rationalize its overall risk profile. Although this may impact a potential alternate source of income, it will significantly reduce IFSL's market risk.
- The substantial loss recognized during FY09 eroded IFSL's equity base, in turn hampering its risk absorption capacity. Consequently, it has reduced IFSL's capacity for handling the targeted growth in brokerage volumes. Nonetheless, the company, in managing its cash flows, continues to draw comfort from stand-by lines of credit available from various financial institutions.

### PROFILE

- IGI Finex Securities Limited (IFSL) is a wholly owned subsidiary of IGI Investment Bank Limited – a Packages Group company. It primarily offers equity, money market, foreign exchange and commodity future brokerage services. The company has its head office in Karachi. Currently, in addition to its 2 branches in Karachi, IFSL is offering its services from 4 branches of IGI Financial Services (IGI FS).
- IFSL has a five-member board of directors, including two independent members. The board comprises qualified and experienced professionals from various fields but with limited direct brokerage industry experience. The CEO, Mr. Azhar Ahmad Batla, an MBA, who took this position in 2009, carries more than 12 years of experience in the local financial industry. A team of experienced professionals assists him.