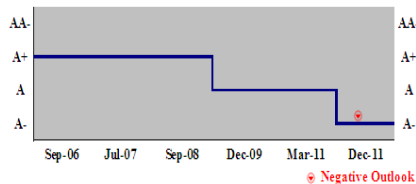


**RATINGS (DECEMBER 2011)**

**KASB SECURITIES LIMITED (KSL)**

	NEW	PREVIOUS
<b>ENTITY</b>		
Long-term	A-	A
Short-term	A2	A1
<b>TFC - Secured, privately placed</b>		
PKR500mln	A	A+
<b>OUTLOOK</b>	Negative	-

**LONG TERM RATING HISTORY**



**FINANCIAL DATA**

PKR (mln)	30-Sep-11*	31-Dec-10
Total Assets	1,873	2,035
Equity	957	1,063
Net Income	(123)	69
Growth in Brokerage Revenue (%)	(16)	(36)
Liquid Assets/ STB + Creditors (%)	60	47

\*Unaudited 9 Months

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**PROFILE**

KSL, listed on KSE since Aug08, is a majority owned subsidiary (77%) of KASB Bank Limited. Lately, a China-based group, Asia International Finance (AIF), has joined the KASB Group. It has injected US\$40mln in KASB Finance, the group's holding company, now equally owned by the KASB Family and AIF. KASB Finance has injected PKR 3,000mln in KASB Bank, now 82% owned by KASB Finance. However, the overall financial profile of KSL's parent - KASB Bank Limited - remains weak. KSL operates through six branches in six cities, Karachi, Lahore, Islamabad, Rahim Yar Khan, Gujranwala and Multan.

**TFC ISSUE**

KSL has issued a secured TFC of PKR 500mln in June 2007, carrying profit at the rate of 6-month KIBOR plus 190bps, payable semi-annually, with no floor and cap. The instrument is secured by way of first ranking pari passu charge on all present and future current assets as well as first ranking charge on present and future fixed asset, with 25% margin. The TFC is due for full redemption on June 27, 2012 and only the final installment of PKR 179mln is outstanding.

**RATING RATIONALE AND KEY DRIVERS**

- The ratings reflect KSL's strong position in the equity broking business emanating from its healthy market share and established brand. This is supplemented by a strong research function and advanced technology infrastructure that draws support from the company's association with Bank of America Merrill Lynch (BAML). However, the overall depressed broking volumes have squeezed the respective business available to KSL, in turn, negative operating margins. The proprietary trading activities, though actively monitored, expose the company to market risk. Furthermore, non-earning assets (significant compared to the company's equity), besides putting pressure on the earning capability, have constrained the liquidity profile of the company. The management, cognizant of the situation, is exerting efforts to convert these non-earning assets, via divestment, into earning resources.
- The negative outlook highlights the continuous pressure on core profitability of the company which could result in further weakening of its business profile. The difficult business environment magnifies the challenge.

**ASSESSMENT**

- Pakistan's brokerage industry is featured by a challenging business environment as reflected by volumes at the country's stock bourses. The brokerage volumes in the ready market declined by 42% YoY by end-Sep11 with an average daily value traded of PKR3,800mln for the year (CY10: PKR6,700mln). Meanwhile, the return on the KSE-100 index for CY11 stood at -7% (CY10: 27%; CY09: 62%). Though certain initiatives, including launch of Margin Trading System, were expected to boost the low volumes, public interest remained meager at large.
- In line with the market dynamics, KSL's brokerage revenues declined by 16% YoY during 9MCY11. However, the company managed to augment its market share to 10% during 9MCY11 from 7% in CY10 by holding seminars, opening two new branches, and launching an aggressive promotion campaign for KASB Direct. The revenue mix is tilted towards brokerage income which contributed 86% to the total operating revenue. Within brokerage revenue local retail clients contributed 54% (CY10: 43%), followed by foreign institutions - 26% (CY10: 41%), local institutions - 20% (CY 10: 15%), and foreign retail clients - less than 0.1% (CY10: 1%). The company's commodities' trading, initiated in Jan11, has shown considerable growth mainly benefiting from low base effect, contributing PKR 10mln to the operating revenue at end-Sep11. Nevertheless, declining brokerage revenue coupled with an impairment loss on investments (PKR 22mln) and provision against doubtful debts (PKR 14mln) exerted downward pressure on the bottom-line. The company posted a loss of PKR 123mln during 9MCY11 as compared to a profit of PKR 69mln during CY10.
- The company holds sizeable non-earning assets of PKR 818mln (85% of equity). This mainly comprises investments in Structured Venture (Private) Limited- a subsidiary (PKR 489mln), KASB Bank Limited - the parent company (PKR 24mln) and unlisted shares of related parties including Al-Jomaih Power (PKR 219mln), New Horizon (PKR 75mln) and KASB Funds (PKR 12mln). These investments, besides putting pressure on the earning capability, have constrained the cashflow position of the company.
- Going forward, the company would focus on further rationalizing its cost structure so as to help it achieve considerable savings in operational expenses. KSL aims to maintain its market share by retaining its current clients and sustaining its foreign clientele by capitalizing on its association with BAML. The company intends to work on various technology based initiatives to further improve its brokerage operations. Furthermore, the company is making efforts to offload the non-earning assets from its balance sheet so as to generate liquidity and create room for earnings growth. However, given the current circumstances, KSL's core profitability is expected to remain under pressure.
- KSL has adequate risk management systems in place. The stock market crisis of 2008 and recent events of breach of internal controls in few brokerage companies has highlighted the need for further strengthening. The company holds a proprietary stock trading book (9MCY11: PKR 187mln; CY10: PKR 153mln) exposing it to market risk. KSL's management has increased its focus on strengthening risk management function. Nevertheless, prudent implementation and monitoring of the risk management framework, encompassing all major risks (credit, market and operational) is a continuing challenge.
- KSL's equity has declined on account of losses recognized over the years. The company was moderately leveraged with Debt to Equity of 36% at end-9MCY11 (CY10: 48%; CY09: 51%). However, KSL's overall financial risk has increased owing to negative profitability. This translates into a low cushion available in the form of liquid assets to further absorb any kind of cashflow shock. The company has lately met its TFC obligation (Installment: PKR 193mln) from its cash reserves (~PKR 100mln), and by utilizing its credit lines. The company had unutilized running finance lines of PKR 1,099mln (PKR 247mln from the parent). Going forward, the company's ability to generate liquidity and secure a regular stream of cashflow would remain imperative.