

**REVIEW OF THE BANKING SECTOR IN PAKISTAN****Performance and Prospects**

**1.1** The commercial banking sector in Pakistan is continuing to perform a critical role in the ongoing economic recovery process. Medium sized banks reinforced their role by achieving better performance in almost all areas including profitability, deposit mobilization and credit expansion. Larger banks, particularly those recently privatized, have embarked upon new initiatives to leverage their inherent strength. In fact, privatization of two major banks (HBL & UBL) is the most significant development of the year. This change is likely to unleash the full potential of these giants and thereby provide a formidable challenge to other private banks in the next two to three years. Meanwhile, foreign banks remain confined to operations in their narrow niche market recording only modest growth both in deposits and advances.

**1.2** Robust deposit growth, relatively higher credit to deposit ratios, lower NPLs, a lagging impact of increasing interest rates on the deposit side, improved fee income on enhanced trade activity and rising stock market are the factors that have played significant role in improving sector profitability. The sector is characterized by intense competition amongst players. This competition has a two-pronged effect: while inducing banks to improve operational efficiency for delivering better services to customers, it has kept pricing under pressure. However, the increasing proportion of SME and consumer financing, with relatively higher margins compared to corporates, has helped in preserving spreads during 2004. Resultantly, the benefit of volume growth was translated into improved core profits. At the same time, the bottom line was flattered by increased income from other sources, particularly through the banks' equities investment portfolios. While the buoyant stock market during most part of the year helped in generating hefty capital gains, the rising interest rates have made some dent in the revaluation gains in banks on their portfolio of government securities.

**1.3** The recent growth trend in deposits is likely to continue. The reverse capital flight, increasing remittances from Pakistanis abroad, and the rapid pace of local wealth creation are likely to keep deposit growth well above nominal GDP growth. Given the existing banking landscape, the medium sized banks are likely to attract relatively higher deposits despite increasing competition from the re-

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invigorated privatized banks. SME and consumer financing are likely to help in maintaining the growth momentum on the asset side. Moreover, corporate lending has also seen significant increases. The ongoing capacity additions in cement, oil, and textiles and the opening of the telecom sector are likely to generate significant credit demand. Further, given recent expansions in textiles, working capital needs of this sector would also be on the higher side. Agriculture sector also offers tremendous growth potential and there is increasing awareness in the entire financial sector about the untapped opportunities. As of last year, most of the banks enthusiastically embarked upon housing finance schemes and hoped to make strong headway in this huge untapped segment. While the potential demand continues to be substantial, the initial enthusiasm – of both borrowers and lenders – has dampened owing to the very sharp increase in real estate prices. This is acting as a deterrent, particularly for the middle-income borrowers, against availing the facilities on offer.

**1.4** After making their historic lows in 2003, the interest rate environment has been on the rise throughout 2004. The rates on the short end have gone up significantly as against the long end resulting in flattening of the yield curve. The central bank, by rejecting bids requiring high returns in recent auctions of long-term bonds, has attempted to rationalize the gap between short-term and long-term interest rates to ensure sustainability of the current economic recovery. Nevertheless, the rising

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inflation and more than targeted broad money growth inevitably calls for a tight monetary policy. Thus, the inclining interest rate trend is likely to continue in 2005 with gradual, though limited, increase. The commercial banking sector will remain a beneficiary of the current environment owing to the fact that most of the advances are based on floating rates whereas the returns on deposits are adjusted after a time lag. However, with increasing interest cost from the perspective of the borrower, banks would face pressure on their pricing in the long run.

**1.5** The trend in improvement of the quality of the asset portfolio continues across the sector. This is being maintained through a combination of recovery/settlements of NPLs and enhanced provisioning. As a consequence, the high proportion of NPLs, which was the major concern of regulators as well as bank managements in the past, is no longer a critical issue. At the same time, however, as most banks venture into relatively un-chartered areas like SME financing, and more particularly, consumer financing, they are exposed to a relatively higher level of potential credit risk. Chastened by the past experience, the State Bank has been proactive in being alert to this risk and is, therefore, in the process of reviewing the prudential regulations to make them consistent with this changing loan portfolio mix. As an example, banks are now obliged to make general provisioning of 1.5% against secured portfolio and 5% against unsecured portfolio of consumer financing. However, for tax purposes a deduction of only upto 3% of income from consumer financing portfolio is allowed. At this stage, it is too early to comment on whether or not the prescribed provisioning is likely to provide adequate coverage against the risk of loss. In the area of consumer financing, the limited track record so far precludes the availability of credible default data which makes it more difficult for banks to determine the potential provisioning requirement. Again, in the area of consumer financing, the lack of a reliable data base on the credit history of individual borrowers continues to be an important constraint even though efforts are in hand to put in place a comprehensive and reliable system providing ready access to all banks.

**1.6** As banks move up the technology ladder, they could become more prone to operational risk. While there is a general awareness about this risk, only a few of the banks have put in place a formalized system for monitoring and controlling operational risk other than strengthening of internal controls principally through the audit committee of the Board.

**1.7** A number of commercial banks have ventured into Islamic banking. This trend is likely to be emulated by most banks. Given the fact that most of the players in this particular niche are not opting for any product innovation, it is unlikely that Islamic banking business would show any exceptional growth in the near-term but could provide a good vehicle for deposit growth.

**1.8** Performance prospects of individual banks would continue to remain a function of a number of bank-specific variables. The asset size of the bank, its geographical outreach, the financial standing and credibility of bank sponsors, the quality of human resource and technological base are all key elements. On the other hand, the relatively smaller banks, who might not have succeeded in developing specific market niches, would continue to fight for survival and might well become candidates for acquisition by or merger with larger banks. Moreover, in pursuance of its policy of boosting the solvency of the banking system, SBP has further raised the minimum capital requirement (PKR 2bln by end-2005), which is likely to provide further stimulus for consolidation. The medium size banks have already come out successfully in the fast evolving competitive environment, and seem well placed for sustaining their performance and asset quality. However, they continue to face the threat of greater competition from the large banks with extensive geographical outreach, as these banks are rapidly overcoming their inefficiencies and are adopting a more market-based business approach. There is, thus, an increasing awareness that, in order to maintain their historic performance, the medium sized banks will have to remain committed to continuous improvement in service quality as well as product innovation. These factors would inevitably lead to greater efficiency in financial intermediation and provide a wider choice to banking customers.

## **Regulatory Framework**

**1.9** The State Bank of Pakistan continues with its proactive role in strengthening the banking sector. Through a combination of regulations and moral suasion, SBP is committed to ensure that the domestic banking sector functions according to the best international practices. In recent years, SBP has demonstrated its commitment and capacity not only at ensuring consolidation and orderly growth in the banking sector, but also introduction of effective risk management policies. The State Bank has recently issued detailed risk management guidelines which elaborate procedures for identifying, measuring, monitoring and managing different risks. Moreover, the SBP, being cognizant

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of the importance of a properly designed and implemented internal control system for an adequate risk management framework, has issued guidelines on internal controls. These guidelines have identified different elements of an internal control system and provide guidance for its implementation, evaluation and reporting. Responsibilities of key players are also highlighted, particularly with regard to the responsibility of BoD for ensuring efficient internal control systems. On a broader front, SBP jointly with SECP is engaged in improving the quality of corporate governance across the entire corporate sector. More specifically, SBP has taken several measures to put in place good governance practices: limiting family representation on the BoD to 25% in case of majority holding, pre-appointment clearance from SBP for CEO and members of the Board, minimum quarterly meetings of the BOD, classification of external auditors in various categories and their rotation, and improving external disclosure and SBP reporting requirements.

**1.10** SBP is in the process of building up capacity internally and within the sector for smooth transition to compliance with capital adequacy requirements of Basel II Accord. Basel II is built on the so-called 'three pillars' of capital adequacy namely: i) the minimum capital requirement, ii) supervisory oversight, and iii) market discipline, based on risk-based disclosure. Pillar 1 requires most attention due to new internal ratings based (IRB) approaches (standardized and advanced) for measuring capital requirements for credit risk. Additionally banks would be required to have sufficient capital to cover market and operational risks, the latter being a new element as the current CAR calculation methodology in Pakistan has no explicit capital charge for operational risk. For calculating capital charge for operational risk, Basel II provides three options, namely i) the Basic Indicator Approach, ii) the Standardized Approach and iii) Advanced Measurement Approach. The role of the central bank (Pillar 2) assumes an even greater importance due to the need of developing technical expertise to review and monitor the banks. Pillar 3 is also significant as the type of risk disclosures go beyond the information currently made publicly available by most Pakistani banks.

**1.11** In line with most other regulators in the region, SBP will follow gradual adoption of Basel II. The central bank has provided a broad roadmap in this regard. Standardized approach for minimum capital calculation for credit risk, and either of the basic indicator or standardized approaches for operational risk will be adopted from 1<sup>st</sup> January

2008. IRB approaches for credit risk will be adopted from 1<sup>st</sup> January 2010. However, detailed guidelines by SBP for implementation of the new accord are awaited.

**1.12** One fundamental innovation under standardized approach is the use of external credit ratings. It moves away from the current practice of a uniform 8% capital charge (100% risk weight) for all finances to varying risk weight (RW) for different credit exposures based on external ratings (AAA & AA categories exposures = 20% RW, A category = 50% RW, BBB & BB categories = 100% RW, B and below categories = 150% RW, and unrated exposures = 100% RW). This is likely to reduce capital requirement to some extent, particularly in the case of banks having large exposures to high rated entities. The higher capital allocation for a low rated exposure would provide incentive for risk based pricing. At the same time, this would encourage the entities, having high credit quality, to obtain credit ratings – PACRA's current rating universe, excluding commercial banks, comprise above 50 rated entities. For claims on banks (local and foreign), the standardized approach provides two options, Option 1 sets charges based on the sovereign rating while Option 2 bases the charge on external rating assigned to the bank. Moreover, off-balance sheet commitments attract a higher conversion factor. Market risk capital charge calculation, as recently adopted by the SBP, is largely unchanged under Basel II. For calculating capital charge for operational risk, the basic indicator approach sets the capital charge at 15% of the average annual gross income for the previous three years and the standardized approach breaks down annual gross income by business lines and different weights are assigned. The calculation of the capital ratio, to be adopted from 1<sup>st</sup> January 2008, is expressed as follows:  $\text{Capital} / [\text{Credit Risk Weighted Assets} + (\text{Operational Risk Charge} \times 12.5) + (\text{Market Risk Charge} \times 12.5)]$ .

**1.13** The IRB framework is calibrated to cover the bank's potential economic losses, namely Expected Loss and Unexpected Loss. The key inputs needed to estimate these losses are Probability of Default (PD), Loss Given Default (LGD), Exposure At Default (EAD) and Maturity (M). The rating system design and data quality are key issues. In PACRA's experience, no Pakistani bank has developed a proper internal grading system and only a few have started thinking about developing such a system. Moreover, no systematically collected and evaluated loss data is available. The level of LGD is crucial in estimating potential losses. However, given a process involving effort of years to recover against



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defaulted loans through repossessions and disposal of collateral, making a reasonable estimate of loss would also be an uphill task. Pakistani banks would need a reasonably longer period (around 3 to 5 years) to develop requisite skills to adopt the IRB approach, which is a fundamental shift to a regulated capital system based on the bank's own internal assessment of its risks. Hence, implementation of IRB approach towards calculating capital requirement requires detailed gap analysis and strong co-ordination between the regulator and banks. The SBP, in consultation with other market players, would need to devise comprehensive guidelines identifying milestones, and explaining actions on part of different players.

PACRA is of the opinion that the adoption of Basel II would require incremental additional capital for most of the banks. The benefit from lower capital allocation on exposures to high rated corporates would not be substantial as in practice only a small portion of a bank's portfolio is externally rated. On the other hand, the banks would have to allocate capital for operational risk, which, though varying, would have an impact in the range of 1 percentage point. Moreover, increasing credit-to-deposit ratio in the recent past has already weakened the capital adequacy structure of most banks, which have resorted to tier 2 capital (unsecured, subordinated TFCs) to meet legal requirements. Nevertheless, the incremental capital requirement is manageable and can be met mostly through high retentions and fresh capital issuances. Moreover, all these measures are expected to promote self-regulation, bring more transparency in the banking sector and augment the banks' risk absorption capacity.

## PACRA RATING ACTIONS

### **April 04, 2005: PACRA Maintains Entity Ratings of First Punjab Modaraba (FPM)**

The Pakistan Credit Rating Agency (PACRA) has maintained the entity ratings of First Punjab Modaraba (FPM) at “A” (Single A) and “A1” (A one) for the long-term and short-term respectively. These ratings denote a low expectation of credit risk and a strong capacity for timely payment of financial commitments.

FPM's ratings reflect its good asset quality and largely sustained performance from core operations. The ratings also take into account the management's strategy for leveraged volume expansion and diversification of the financing portfolio. The management, at the same time, is cognizant of risks arising from its rapid growth stance and is, therefore, continuously improving its control systems.

**About the Modaraba:** Established in 1992, FPM is a perpetual, multi-purpose Modaraba, listed on the Karachi, Lahore and Islamabad stock exchanges. Punjab Modaraba Services (Pvt) Ltd – a wholly owned subsidiary of The Bank of Punjab – holding around 38% stake in the Modaraba manages the Modaraba. The Bank of Punjab was established towards the end of 1989 under the Bank of Punjab Act, with its head office in Lahore. It is a large commercial bank in which the Government of Punjab holds majority stake. The Modaraba is primarily engaged in *morabaha* and lease financing and operates from a single location in Lahore. The Modaraba is targeting an aggressive growth by identifying new market niches, thereby providing facilities to consumer and SME sectors. To facilitate the

future growth it plans to improve its geographical outreach. These reforms are expected to diversify the Modaraba's customer and product base going forward.

### **March 29, 2005: PACRA Maintains Entity Ratings of Soneri Bank Limited and Assigns Rating to its Proposed TFC Issue**

The Pakistan Credit Rating Agency (PACRA) has maintained the long-term and short-term entity ratings of Soneri Bank Limited at ‘AA-’ (Double A minus) and ‘A1+’ (A one plus), respectively. These ratings, applicable to senior unsecured creditors (depositors) of the bank, denote a very low expectation of credit risk emanating from a very strong capacity for timely payment of financial commitments

The proposed unsecured, subordinated term finance certificates issue of PKR 1,200mln by Soneri Bank Limited has been assigned a rating of ‘A+’ (Single A plus). The rating denotes a low expectation of credit risk emanating from a strong capacity for timely payment of financial commitments.

The ratings reflect the bank's prudent stance towards risk, demonstrated in its very good asset quality, while continuing a steady asset growth, thereby maintaining its sector share of around 2%. The ratings also take into account the bank's recently initiated comprehensive plan to further strengthen its risk management systems.

**About the issuer – the bank:** SBL, operating a countrywide branch network of 52 branches,

commenced its operations in 1992. The Feerasta family, owners of the Rupali group, holds the controlling stake in the bank. The group's primary activities are centered on the synthetic textile industry. The group, through Ferrasta family members and nominees, maintains a dominant position on the bank's board of directors. The bank's main activities are short-term lending, mainly foreign trade related financing and running finance. These activities are mainly focused in the corporate sector, followed by SMEs. The President and Chief Executive, a banker with over four decades of domestic and international banking exposure, manages the operations of the bank through a team of experienced professionals.

**About the issue:** The proposed unsecured subordinated TFCs would have a tenor of 8 years carrying mark-up, payable semi-annually, at a floating rate of latest 6-month KIBOR plus 1.6%. The principal will be redeemed in four equal semi-annual installments starting from the 78 th month from the issue date.

### **March 18, 2005: PACRA Maintains the Ratings of Nishat Mills Limited (NML)**

The Pakistan Credit Rating Agency (PACRA) has maintained the long-term rating at ‘A+’ (Single A Plus) and the short-term rating at ‘A1’ (A One) of Nishat Mills Limited. These are applicable to the senior unsecured creditors of the entity. The secured TFC issue of PKR 600mln, due for final redemption in September 2005, has been assigned a short-term rating of ‘A1’ (A One). These ratings denote a low expectation of credit risk

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emanating from a strong capacity for timely payment of financial commitments.

The ratings reflect the ability of the company to generate stable core earnings despite a difficult operating environment, arising from the company's strong competitive edge and reduced risks to market volatility. This emanates from the diverse product and customer base, increased focus on value-addition and superior customer relations. The improving dividend income stream from associated companies also augurs well for future performance. Further, NML's conscious efforts towards preparation for the challenges as well as the opportunities following the termination of the quota regime are also a critical rating factor.

**About the TFC Issue:** NML issued secured TFCs of PKR 600mln in FY01 of 4-year tenor with profit payable semi-annually, while principal payable in 4 equal semi-annual installments commencing in Mar04. The profit payment is based on SBP discount rate Plus 150bps with a floor of 13% and a cap of 17%. The TFCs are secured by way of a ranking charge of PKR 750mln on fixed assets (excluding immovable properties) of the company, providing 25% margin.

**About the Corporation:** Nishat Mills Limited (NML) is the single largest textile composite unit in Pakistan, with an installed capacity of 182,568 spindles and 586 Looms, including 472 high-speed Airjet looms. The company is a leading exporter of textile products having extensive spinning, weaving, dyeing, printing, finishing and stitching facilities. NML is the flagship company of the Nishat Group of Companies – one of the largest conglomerates with interests in the textiles, cement and financial sector. The Nishat Group family members and associated

concerns collectively hold around 44% of NML's equity.

NML's product range is composed of various varieties of yarn, grey fabric, processed fabrics and made-ups. The bulk of its earnings, 83% of total sales, are export-based.

### **March 16, 2005: PACRA Assigns Ratings to Attock Refinery Limited (ARL)**

The Pakistan Credit Rating Agency (PACRA) has assigned a long term rating of 'AA-' (Double A Minus) and a short term rating of 'A1+' (A One Plus) to Attock Refinery Limited. The ratings, applicable to the senior unsecured creditors of the company, denote a very low expectation of credit risk emanating from a very strong capacity for timely payments of financial commitments.

The ratings reflect ARL's sustained robust performance over the years in a high-volume, low-margin industry that is subject to volatile input and output prices. The ratings also take into account the company's very strong financial profile emanating from a virtually debt free capital structure and strong liquidity. This substantially mitigates the element of financial risk. Moreover, the strengthening equity base due to mandatory minimum 50% profit retention would continue to provide significant cushion against any future unforeseen events. Nevertheless, the company remains exposed to the cyclical nature of refining margins. However, this concern is somewhat mitigated by the recent upturn in the refining industry coupled with higher expected international oil prices. The ratings also factor in the benefits accruing to the company from its association with the only fully integrated group in the petroleum sector of the country.

**About the company:** Attock Oil Company Limited (AOC), incorporated in UK and a pioneer in oil refining in South Asia, started refining operations in Pakistan in 1922. ARL was incorporated in 1978 to take over the crude oil refining business from AOC, which has 52.5% shareholding in ARL. ARL is listed on all the three stock exchanges of the country and currently has refining capacity of 37,500 BPD. The company's refinery is strategically located up-country in the north of Pakistan and caters to the petroleum products requirements in its region of location.

The company is a member of the Attock Group of Companies, a fully integrated group covering all segments of oil and gas industry from exploration, production, and refining to marketing of a wide range of petroleum products. In Pakistan, the Attock Group has considerable representation in the petroleum sector through its exploration companies – Attock Oil Company Limited and Pakistan Oilfields Limited – and an oil marketing company – Attock Petroleum Limited – in addition to the refining company.

### **March 08, 2005: PACRA Assigns Entity Ratings to Investment Corporation of Pakistan (ICP)**

The Pakistan Credit Rating Agency (PACRA) has assigned a long-term entity rating of "AA" (Double A) to ICP and maintained its short-term rating at "A1+" (A one plus). These ratings, applicable to senior unsecured creditors, denote a very low expectation of credit risk and a very strong capacity for timely payment of financial commitments.

ICP's rating reflects the Corporation's practically risk-free profile, emanating from a

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completely depleted financing portfolio. The rating also factors in its substantially diminished credit risk through adequate provisioning and continuing recoveries. The liquidity provided by substantial capital gains, augmenting the capacity of the Corporation to honour its short-term liabilities in a timely manner, is also a key factor.

The Corporation is currently performing limited operations while awaiting a decision from the Privatization Commission with regard to its privatization process as an ongoing concern. The exact time frame for completion of the process has not yet been indicated. PACRA is, therefore, assigning the ratings with the assumption that until the privatization process is completed ICP will continue to function with its current operations and not venture into any new business activities that could enhance the risk exposure.

**About the Corporation:** Investment Corporation of Pakistan (ICP) – a state-controlled Development Finance Institution – was established through the ICP Ordinance 1966. The main objective of ICP was to strengthen the capital market in Pakistan, primarily through encouraging broader participation in listed equity securities. ICP performed its core functions satisfactorily up until the late eighties when its financial position began to deteriorate after entering into project financing activity. High incidence of non-performing loans and slump in the stock market led ICP to a liquidity crunch and the Government decided to wind up the Corporation. The Privatization Commission (PC), however, had recommended the privatization of ICP in April 2003, and in March 2004 it appointed financial and legal advisors for the ICP privatization transaction. The advisors have submitted their

report to the PC and ICP management is of the view that the PC is actively engaged in the privatization process of the Corporation.

**March 02, 2005: PACRA Maintains the Ratings of Orix Investment Bank Limited**

The Pakistan Credit Rating Agency (PACRA) has maintained the long-term and short-term entity ratings of Orix Investment Bank Pakistan Limited (OIBPL) at 'A' and 'A1' respectively. These ratings, applicable to senior unsecured creditors of the bank, indicate a low expectation of credit risk and a strong capacity for timely payment of financial commitments.

The ratings of OIBPL reflect virtually maintained overall risk profile with declining trend in the bank's profitability. The ratings also recognize the management's efforts at diversifying the revenue stream to arrest this trend. Meanwhile, the implicit support from the parent group has also been factored in.

**About the bank:** ORIX Investment Bank Pakistan Limited (OIBPL) was incorporated in July 1995 and commenced operations during the 2Q 1996, with a paid-up capital of PKR 200 mln that was further enhanced to PKR 300 mln by way of rights issue during FY2003. OIBPL is listed on the Karachi and Lahore Stock Exchanges of Pakistan. The main sponsors of OIBPL are ORIX Corporation of Japan (OCJ) and ORIX Leasing Pakistan (OLP) with 20% and 15% shareholding respectively. The other shareholders include local and foreign financial institutions and individuals.

The bank's core business activities include short-term lending, fund

placements, treasury operations, money market brokerage, equity broking and financial and advisory services.

**February 18, 2005: PACRA Upgrades Long-term Rating of First Fidelity Leasing Modaraba (FFLM)**

The Pakistan Credit Rating Agency (PACRA) has upgraded the long-term rating to 'A-' (Single A minus), while maintaining the short-term rating at 'A2' (A two) of First Fidelity Leasing Modaraba (FFLM). These ratings denote a low expectation of credit risk and a strong capacity for timely payment of financial commitments.

The ratings reflect FFLM's strengthened risk absorption capacity, mainly emanating from substantially improved asset quality and adoption of low risk growth strategy based on a low-leveraged capital structure. The ratings also take into account diversified sources of revenue, an outcome of recent acquisition of a brokerage business and focus on property investment, which are likely to add sustainability to income, going forward.

**About the Modaraba:** FFLM, listed on all the three stock exchanges of the country, was established in 1991 and is managed by Fidelity Capital Management (Pvt.) Limited (FCML), which is part of the Crescent Group. The Crescent Group is one of the well-known corporate groups in Pakistan with diverse interests both in manufacturing and financial services.

The management, subsequent to the merger of First Hajvery Modaraba and Fidelity Securities (Pvt.) Limited, has revisited its strategy and identified three main areas for its operations namely

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leasing, brokerage business and asset (property) management.

### **February 10, 2005: PACRA Maintains Entity & TFC Ratings of First Dawood Investment Bank Limited**

The Pakistan Credit Rating Agency (PACRA) has maintained the long-term rating at "A+" (Single A plus), and the short-term rating at "A1" (Single A One) of First Dawood Investment Bank Limited (FDIB). These ratings are applicable to senior unsecured creditors and denote a low expectation of credit risk emanating from a strong capacity for timely payment of financial commitments.

The ratings of two tranches of secured TFCs of PKR 253mln and PKR 345mln have also been maintained at "AA-" (Double A minus). This rating denotes a very low expectation of credit risk emanating from a very strong capacity for timely payments of financial commitments.

FDIB's ratings reflect the management's ongoing diversification efforts aimed at making the bank more competitive and less prone to adverse conditions in any one of its business segments. This has helped in improvement in the asset quality. Meanwhile, exposure to volatility risk remains high, an outcome of an increased level of non-strategic investments that are vulnerable to market conditions.

**About the TFC Issues:** The bank has issued TFCs worth PKR 598mln. The first tranche of PKR 253mln was issued in September 2001. It carries interest at 175bps plus the SBP discount rate with a floor of 13.5% and a ceiling of 17.5% payable semi-annually. The second tranche of PKR 345mln was issued in July 2002 at similar rate, but with a floor of 12.25% and a ceiling of 16.25% payable semi-annually.

These instruments are of a perpetual nature, and have been issued initially for a tenor of five years till a call and put option is exercised. The TFCs are secured by way of registered charge over all present and future assets and receivables of FDIB with a margin of 20%.

**About the bank:** Dawood Leasing Company Limited, operating since 1995, was converted into First Dawood Investment Bank (FDIB) in 2004. This was done in order to enable the entity to offer a wide range of financial services. The company has undergone a paradigm shift, with investment banking gradually displacing leasing as the management's core focus with further expansionary plans in the pipeline.

### **January 28, 2005: PACRA Assigns Rating to the Proposed Securitised TFC Issue of Chanda Oil & Gas Securitisation Company Limited (COGSCL)**

The Pakistan Credit Rating Agency (PACRA) has assigned a rating of 'A' (Single A) to the proposed asset-backed term finance certificates issue of PKR 1,000mln by Chanda Oil and Gas Securitization Company Limited (COGSCL). The rating denotes a low expectation of credit risk emanating from a strong capacity for timely payments of financial commitments. The cash flows from sale of production of Chanda oilfield are considered adequate to allow COGSCL to meet the contractual TFC obligations comfortably.

**About the Issuer:** COGSCL is a bankruptcy-remote special purpose vehicle. It will acquire the title, property and right in receivables of Zaver Petroleum Corporation Limited (ZPCL) originating from sales of ZPCL's share of production

from the Chanda oilfield. The transaction between COGSCL and ZPCL will be a true sale. COGSCL will generate the funds required to purchase the receivables through issuing asset backed term finance certificates and will create a first exclusive charge over the receivables in favour of the trustee.

**About the Instrument:** The TFC will have a tenor of 7 years including grace period of 6 months carrying profit based on simple average of last 7 days of ask side of 3 months KIBOR rate plus 325 bps with a floor of 8.95% p.a. and a cap of 13% p.a. Principal redemption will be in 27 unequal quarterly instalments commencing from the end of grace period.

**About the Originator:** ZPCL, incorporated in August 1991, is a local exploration and production company. Hashoo Group owns the majority stake in ZPCL through its different companies and individual nominees. The group has diversified business interests, out of which Pearl-Continental Hotel and Marriott Hotel chains are the most significant. ZPCL has 10.5% working interest in Chanda oilfield, shared with OGDCL (72%) and Government Holdings (Pvt.) Limited (17.5%). The company plans to utilize the funds raised through securitized TFC for its core operations and for debt re-profiling.

### **January 26, 2005: PACRA Maintains TFC Rating of Maple Leaf Cement Factory Limited (MLCFL)**

The Pakistan Credit Rating Agency (PACRA) has upgraded the rating of the secured TFCs of PKR 250mln of Maple Leaf Cement Factory Limited to 'A+' (Single A Plus). The rating denotes a low expectation of credit risk emanating from a strong capacity for timely payments of financial commitments.

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The rating reflects the healthy internal cash generation on the back of significant improvement in profitability. The rating also takes into account the planned right and preference shares issues, which are expected to substantially improve the financial structure of the entity over the remaining tenor of TFCs.

**About the TFC Issue:** TFCs of PKR 250mln were issued in Jul 02 to meet the cost of a new coal grinding system. The tenor of the instrument is four years and the profit rate is five years' PIB rate + 250bps subject to a floor of 15.25% and a ceiling of 17.75%. While the profit is payable semi-annually, the redemption of the principal is in six equal installments commencing in Jan 04. The issue is secured by way of a first pari passu charge on the present and future fixed assets (excluding land and buildings) of the company.

**About the company:** Maple Leaf Cement Factory Limited (MLCFL) is one of the largest cement factories in Pakistan, with an overall annual production capacity of around 1.5mln tons. The company has a diversified product range and is the only cement company in Pakistan capable of producing grey, white, sulphate resisting and low alkali cement.

MLCFL is a part of the Kohinoor Maple Leaf Group, which is one of the leading textile manufacturers of the country. Kohinoor Textile Mills Limited holds 50.13% shareholding in MLCFL. While effectively family controlled, MLCFL is run by professional management. The main sponsor, who is also the chief executive of the company is a leading industrialist. Presently, he is chairman of the group and mainly responsible for making policy decisions and giving commercial guidelines.

### **January 14, 2005: PACRA Upgrades Long-term Entity Rating of Orix Leasing Pakistan Limited (OLP)**

The Pakistan Credit Rating Agency (PACRA) has upgraded the long-term entity rating of Orix Leasing Pakistan Limited (OLP) to 'AA+' (Double A Plus), while maintaining the short-term rating at 'A1+' (A One Plus). These ratings, applicable to senior unsecured creditors of the company, indicate a very low expectation of credit risk and a very strong capacity for timely payment of financial commitments.

OLP's first tranche of TFCs (PKR 742mln), due for final redemption in April 2005, has been assigned a short-term rating of 'A1+' (A One Plus) and the rating of second tranche of TFCs (PKR 758mln) is maintained at 'AA+' (Double A Plus).

The ratings reflect OLP's demonstrated ability to sustain its performance and low-risk asset profile, while maintaining its leadership in the sector. The company continues to follow a policy of diversification and product innovation. The ratings also recognize the outstanding professional management team, with a track record of successfully implementing well-designed business plans. The implicit support of Orix Corporation, Japan is also a key factor.

**About the TFC Issues:** The first tranche of PKR 742mln was issued in April 2001 for a tenor of 4years carrying interest at 14% payable semi-annually. The second tranche of PKR 758mln was issued in August 2002 for a tenor of 4years with bullet payment of principal with a coupon rate of SBP discount plus 2% with a floor of 10% and cap of 13% payable semi-annually. These are secured by way of registered charge over specific

leased assets and their related receivables.

**About the company:** Orix Leasing Pakistan Limited (OLP), the largest leasing company in the country, commenced operations in 1987. It has reasonable geographical coverage through its 14 independent branches and desks at 11 UBL branches. Orix Corporation, Japan, OLP's major shareholder, has a consolidated asset base exceeding US\$ 51bln as at September 30, 2004 with operations in 24 countries.

### **January 03, 2005: PACRA Maintains the Ratings of Askari Leasing Limited (ALL)**

The Pakistan Credit Rating Agency (PACRA) has maintained the long-term rating at 'A+' (Single A plus) and the short-term rating at 'A1' (A one) of Askari Leasing Limited (ALL). These are applicable to the senior unsecured creditors of the company. These ratings denote a low expectation of credit risk and a strong capacity for timely payment of financial commitments.

The ratings reflect ALL's sustained performance despite an increasingly competitive operating environment. The ratings also take into account the high gearing as compared to peers and its continuing impact on the risk absorption capacity.

**About the company:** ALL was incorporated in August 1993 and is listed on all three stock exchanges of the country. AWT is the majority shareholder of ALL since its inception, followed by financial institutions and individuals. AWT was established in 1971 and has over the years evolved into one of the largest business conglomerates of the country, with business concerns in sugar processing, textiles, real estate development, commercial banking, leasing, cement, general insurance and travel services. In the financial



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sector, AWT is represented by a leading commercial bank, a leasing company and a general insurance company. The Board of Directors of ALL includes seven nominees of AWT, while one director is nominated by the National Investment Trust.

ALL continued to be the second largest leasing company in FY04 in the leasing sector, in terms of both NIL and total assets, with a market share of over 13% in terms of NIL, and with a relatively extensive branch network. In the last couple of years, that is, with the assumption of office by the current chief executive, the branch operations have been strengthened through decentralization, which ensures greater synergy with Askari bank branches.



## List of Publicly Disseminated Ratings

### Entity Ratings:

	Name of the Organisation	Type of Rating	Date of Notification MM/DD/YYYY	Rating Assigned		
				FS/FR/ AMR/DG	Long-Term    Short-Term	
<b>FINANCIAL SECTOR</b>						
<b>MUTUAL FUNDS / ASSET MANAGEMENT COS.</b>						
1.	ABAMCO Limited	AMR <sup>1</sup>	06/30/2004	AM2	---	---
2.	Arif Habib Investment Management Limited	AMR	09/24/2004	AM2	---	---
3.	Atlas Asset Management Company Limited	AMR	10/27/2004	AM3	---	---
4.	BSJS Balanced Fund Limited	FR <sup>2</sup>	05/17/2004	AA(f)	---	---
5.	National Investment (Unit) Trust – NIT	FR	09/15/2003	AA(f)	---	---
6.	Pakistan Income Fund (PIF)	FR	09/24/2004	A+(f)	---	---
7.	Pakistan Premier Fund (PPF)	FR	09/24/2004	AA(f)	---	---
8.	Pakistan Stock Market Fund (PSMF)	FR	09/24/2004	AA(f)	---	---
9.	Unit Trust Of Pakistan	FR	04/01/2004	AA(f)	---	---
<b>DFIS / INVESTMENT COS. / BROKERAGE HOUSES</b>						
1.	House Building Finance Corporation	Entity	10/06/2004		A	A1
2.	Investment Corporation of Pakistan (ICP)	Entity	03/04/2005		AA	A1+
3.	Jahangir Siddiqui & Company Limited	Entity	01/16/2004		AA+	A1+
4.	Pakistan Industrial Credit & Investment Corporation Limited (PICIC)	Entity	06/29/2004		AA	A1+
5.	Pakistan Kuwait Investment Company (Pvt) Limited	Entity	06/30/2004		AAA	A1+
6.	Pak Libya Holding Company (Pvt) Limited	Entity	06/30/2004		AA-	A1+
<b>MODARABAS</b>						
1.	First Fidelity Leasing Modaraba	Entity	02/08/2005		A-	A2
2.	First Habib Modaraba	Entity	12/17/2004		AA	A1+
3.	First Punjab Modaraba	Entity	12/31/2004		A	A1
4.	Standard Chartered Modaraba (Formerly First Grindlays Modaraba)	Entity	12/22/2004		AA+	A1+
<b>LEASING COMPANIES</b>						
1.	Askari Leasing Limited	Entity	12/30/2004		A+	A1
2.	Network Leasing Corporation Limited	Entity	12/17/2004		BBB	A3
3.	Orix Leasing Pakistan Limited	Entity	01/12/2005		AA+	A1+
4.	Trust Leasing Corporation Limited	Entity	11/12/2004		AA-	A1+
5.	Union Leasing Limited	Entity	12/22/2004		A+	A1
<b>BANKING COMMERCIAL</b>						
1.	AlBaraka Islamic Bank (Pakistan Branches)	Entity	06/21/2004		A-	A1

<sup>1</sup> Asset Manager Rating

<sup>2</sup> Fund Rating



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	Name of the Organisation	Type of Rating	Date of Notification MM/DD/YYYY	Rating Assigned	
				FS/ FR/ AMR/DG	Long-Term Short-Term
2.	Askari Commercial Bank Limited	Entity	06/24/2004	AA+	A1+
3.	Bank Al Habib Limited	Entity	06/23/2004	AA	A1+
4.	Bank Alfalah Limited	Entity	06/24/2004	AA	A1+
5.	The Bank of Punjab	Entity	06/23/2004	A+	A1
6.	First Women Bank Limited	Entity	10/15/2004	AA	A1+
7.	KASB Bank Limited	Entity	04/23/2004	BBB+	A2
8.	Metropolitan Bank Limited	Entity	06/22/2004	AA+	A1+
9.	Muslim Commercial Bank Limited	Entity	06/19/2004	AA	A1+
10.	NDLC-IFIC Bank Limited	Entity	07/29/2004	A-	A2
11.	Prime Commercial Bank Limited	Entity	06/28/2004	A+	A1
12.	Saudi Pak Commercial Bank Limited	Entity	06/30/2004	BBB	A3
13.	Soneri Bank Limited	Entity	03/18/2005	AA-	A1+
14.	Union Bank Limited	Entity	06/30/2004	A+	A1

## BANKING INVESTMENT

1.	Atlas Investment Bank Limited	Entity	12/22/2004	A+	A1
2.	First Dawood Investment Bank Limited (Formerly Dawood Leasing Company Limited)	Entity	02/03/2005	A+	A1
3.	First International Investment Bank Limited	Entity	12/22/2004	A	A1
4.	Jahangir Siddiqui Investment Bank Limited	Entity	02/23/2004	A+	A1
5.	Orix Investment Bank Limited	Entity	12/29/2004	A	A1

## INSURANCE COMPANIES

1.	Habib Insurance Company Limited	IFS <sup>1</sup>	09/21/2004	A	---	---
2.	International General Insurance Company of Pakistan Limited (IGI)	IFS	06/23/2004	AA	---	---
3.	Muslim Insurance Company Limited	IFS	09/23/2004	A	---	---
4.	New Jubilee Insurance Company Limited (NJI)	IFS	09/27/2004	AA	---	---

## REAL ESTATE DEVELOPERS & PROJECTS

1.	Eden Developers (Pvt) Limited	DG <sup>2</sup>	07/01/2004	PE2	---	---
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## INDUSTRIAL CORPORATES

### TEXTILE

1.	Azgard Nine Limited (Formerly Legler Nafees Denim Mills Limited)	Entity	02/25/2004	A	A1
2.	Nishat Mills Limited	Entity	03/01/2005	A+	A1

### SUGAR & ALLIED

1.	Al-Abbas Sugar Mills Limited	Entity	04/12/2004	A-	A2
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### FUEL & ENERGY

1.	Attock Petroleum Limited (APL)	Entity	11/14/2004	AA	A1+
2.	Attock Refinery Limited (ARL)	Entity	03/02/2005	AA-	A1+

<sup>1</sup> Insurer Financial Strength Rating

<sup>2</sup> Developer Grading



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Name of the Organisation	Type of Rating	Date of Notification	Rating Assigned	
			Long-Term	Short-Term
3. Pak-Arab Refinery Company Limited (PARCO)	Entity	03/31/2004	AAA	A1+
4. Pakistan State Oil Company Limited (PSO)	Entity	10/20/2004	AAA	A1+
<b>TRANSPORT &amp; COMMUNICATION</b>				
1. Pakistan Mobile Communications (Pvt) Limited (Mobilink)	Entity	09/23/2004	AA-	A1
2. WorldCall Communications Limited	Entity	04/22/2004	A+	A1
<b>CHEMICAL &amp; PHARMACEUTICALS</b>				
1. Engro Chemical Pakistan Limited	Entity	06/14/2004	AA-	A1+
<b>PAPER &amp; BOARD</b>				
1. Packages Limited	Entity	04/23/2004	AA	A1+
<b>MISCELLANEOUS</b>				
1. Tri-Pack Films Limited	Entity	05/14/2004	A+	A1



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## Term Finance Certificates (TFCs) Ratings:

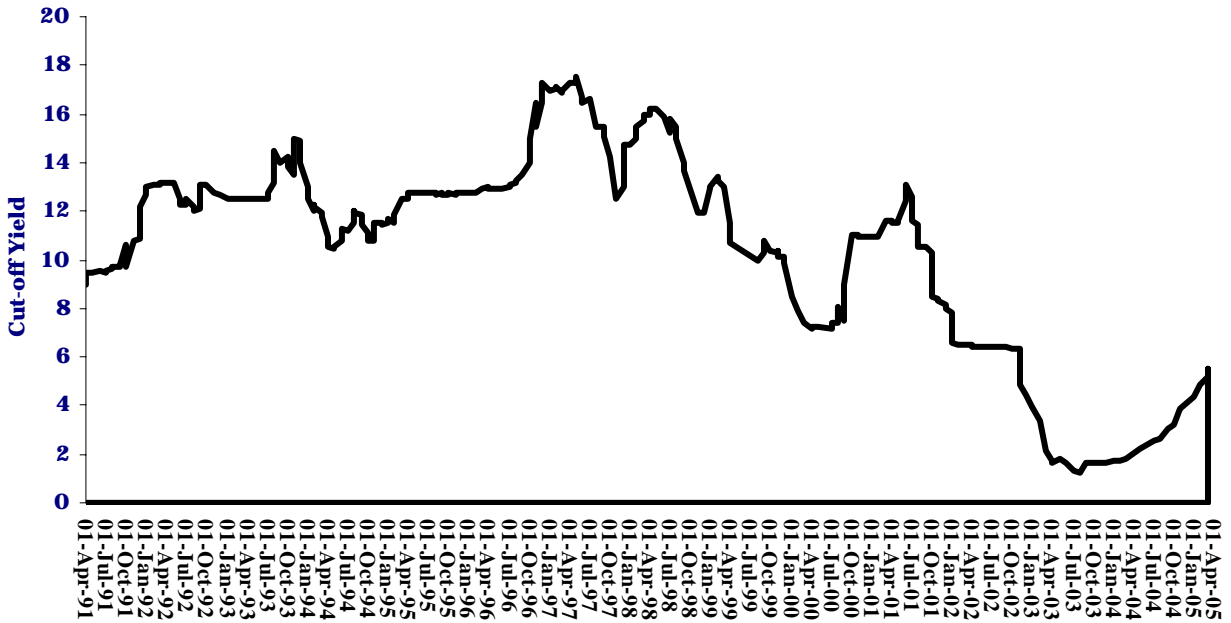
	Name of the Organisation	Amount PKR (mln)	Date of Notification (MM/DD/YYYY)	Date of Issue (MM/DD/YYYY)	Rating Assigned
1.	Al-Abbas Sugar Mills Limited ( <i>Privately Placed</i> )	350.00	02/17/2005	07/03/2003	A+
2.	Al-Noor Sugar Mills Limited	203.66	04/23/2004	10/31/2000	BBB+
3.	Askari Commercial Bank Limited	1,500.00	12/17/2004	02/04/2005	AA
4.	Atlas Investment Bank Limited – I	200.00	12/22/2004	09/27/2000	AA-
5.	Atlas Investment Bank Limited - II	100.00	12/22/2004	08/16/2001	AA-
6.	Bank Al Habib Limited	1,350.00	06/23/2004	07/16/2004	AA-
7.	Bank Alfalah Limited – I	650.00	06/24/2004	12/21/2002	AA-
8.	Bank Alfalah Limited – II	1,250.00	08/26/2004	11/24/2004	AA-
9.	Chanda Oil & gas Securitisation Company Limited – (Securitized)	1,000.00	06/08/2004	02/16/2005	A
10.	Engro Chemical Pakistan Limited (2 <sup>nd</sup> Tranche)	1,000.00	04/05/2005	07/06/2002	AA+
11.	First Dawood Investment Bank Limited ( <i>Formerly Dawood Leasing Company Limited</i> ) (1 <sup>st</sup> Tranche)	253.05	02/03/2005	09/21/2001	AA-
12.	First Dawood Investment Bank Limited ( <i>Formerly Dawood Leasing Company Limited</i> ) (2 <sup>nd</sup> Tranche)	345.00	02/03/2005	07/27/2002	AA-
13.	First International Investment Bank Limited (M-Series)	57.04	12/22/2004	09/01/2001	A1*
14.	Gulistan Textile Mills Limited	320.67	04/26/2004	09/05/2001	A-
15.	Jahangir Siddiqui & Company Limited – I	500.00	01/16/2004	04/18/2003	AA+
16.	Jahangir Siddiqui & Company Limited – II	500.00	09/15/2004	12/23/2004	AA+
17.	Maple Leaf Cement Factory Limited	250.00	01/10/2005	07/20/2002	A+
18.	Muslim Commercial Bank Limited	1,600.00	06/19/2004	08/10/2002	AA-
19.	Network Leasing Corporation Limited	100.00	12/17/2004	10/08/2000	A2*
20.	Nishat Mills Limited	600.00	03/01/2005	09/19/2001	A1*
21.	Orix Leasing Pakistan Limited (1 <sup>st</sup> Tranche)	742.00	01/12/2005	04/07/2001	AA+
22.	Orix Leasing Pakistan Limited (2 <sup>nd</sup> Tranche)	758.00	01/12/2005	08/01/2002	AA+
23.	Prime Commercial Bank Limited	800.00	10/20/2004	02/12/2005	A
24.	Securetel SPV Limited – (Securitized)	850.00	11/26/2004	04/27/2003	A
25.	Shahmurad Sugar Mills Limited	230.00	04/26/2004	05/21/2002	BBB
26.	Soneri Bank Limited	1,200.00	03/18/2005	<i>To be issued</i>	A+
27.	Sui Southern Gas Company Limited (1 <sup>st</sup> Tranche)	1,000.00	01/06/2005	06/01/2001	AA
28.	Sui Southern Gas Company Limited (2 <sup>nd</sup> Tranche)	1,250.00	01/06/2005	06/11/2002	AA
29.	Trust Leasing Corporation Limited – I	250.00	11/12/2004	06/03/2003	AA
30.	Trust Leasing Corporation Limited – II	375.00	11/12/2004	07/18/2004	AA
31.	Union Bank Limited – I	750.00	06/30/2004	12/21/2002	A
32.	Union Bank Limited – II	750.00	06/30/2004	01/20/2004	A
33.	Union Leasing Limited	357.10	12/22/2004	04/20/2002	A1+*
34.	WorldCall Communications Limited	350.00	04/22/2004	10/01/2002	AA-
<b>Total Amount Issued:</b>		21,791.42			

\* Short-term rating

## INTEREST RATE TRENDS

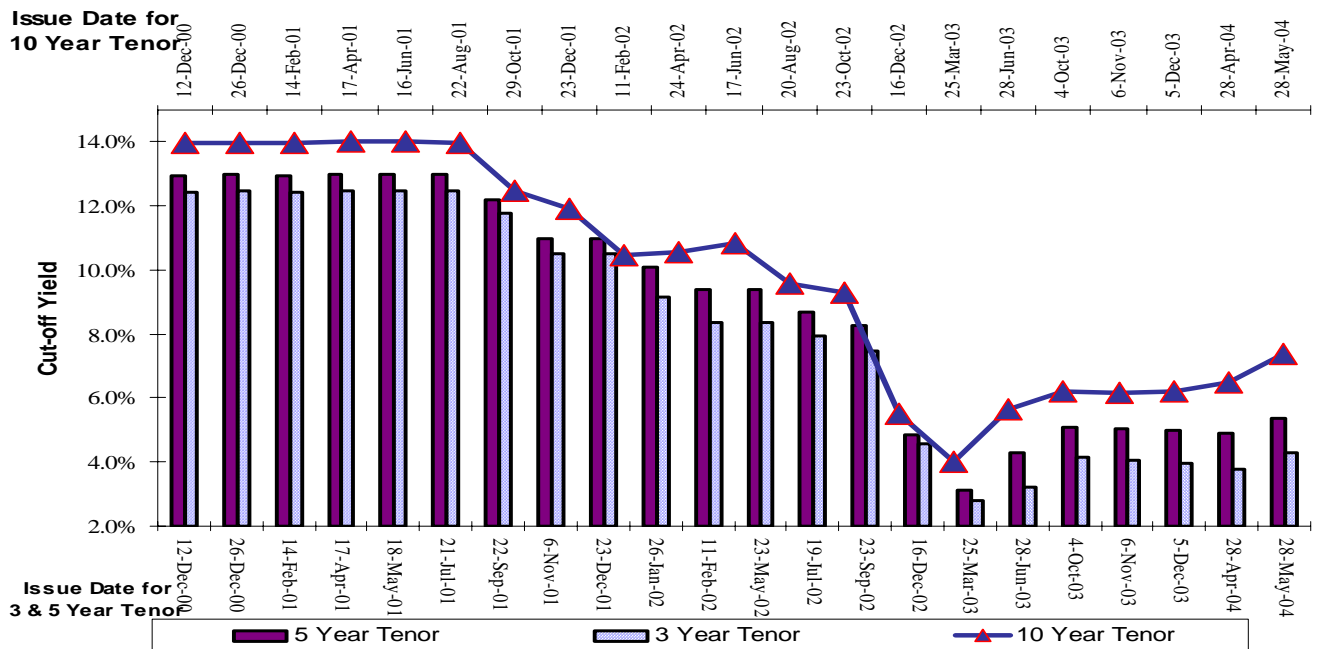
### Short Term: (Treasury Bills)

6-Month Treasury Bills Cut-Off Yield



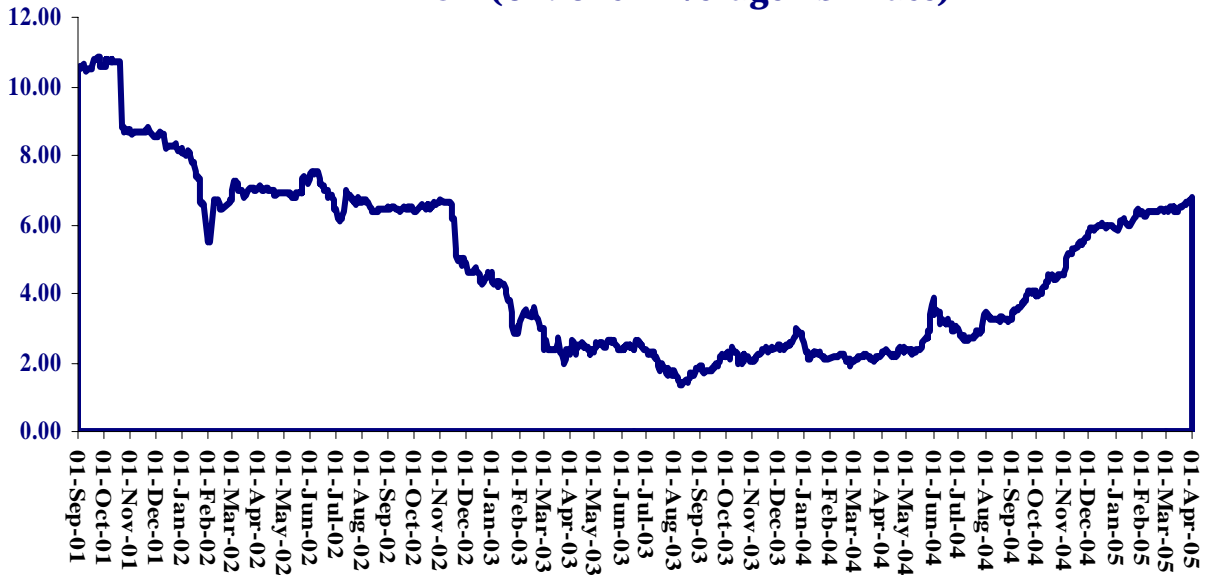
### Long Term: (PIBs)

Rates for 3, 5 & 10 Year Tenor



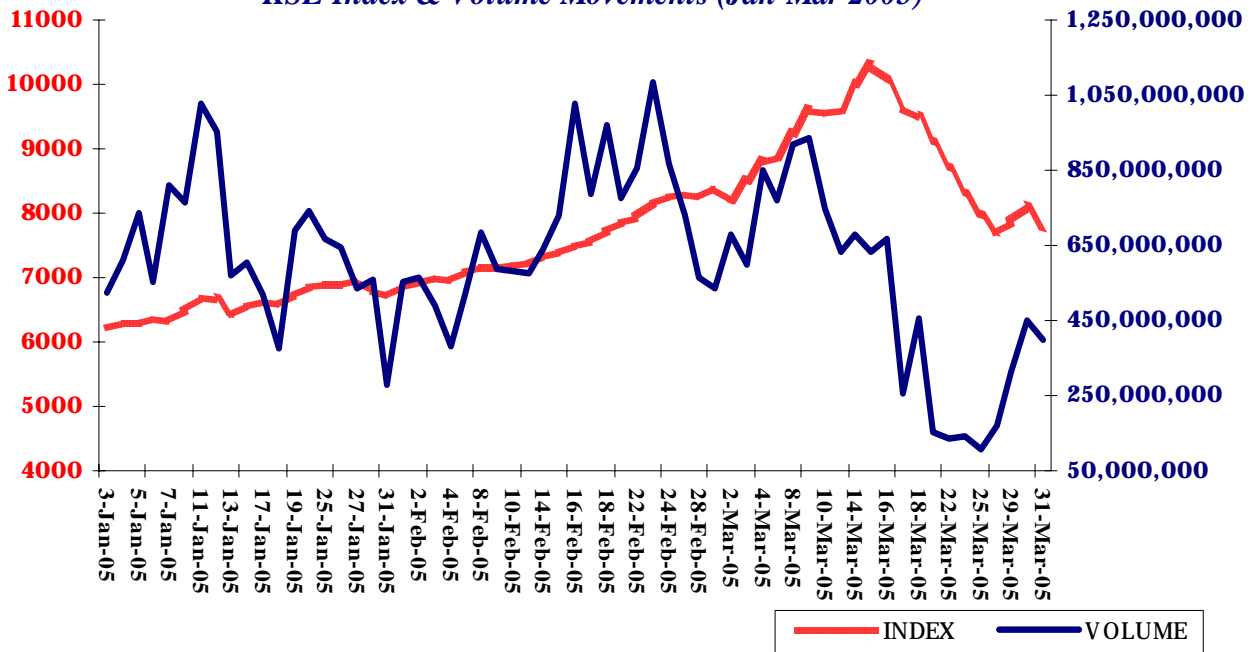
## KIBOR:

### KIBOR (6-Month Average Ask Rate)



## KSE-100 Index:

### KSE Index & Volume Movements (Jan-Mar 2005)





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