The Pakistan Credit Rating Agency Limited

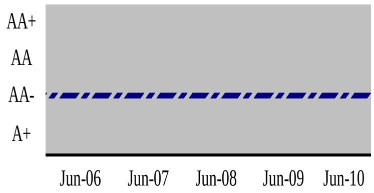
DEVELOPMENT FINANCE

RATINGS (OCTOBER 2010)

PAKLIBYA HOLDING COMPANY (PVT.) LIMITED

RATINGS	NEW	PREVIOUS
Entity		
Long-Term	AA-	AA-
Short-Term	A1+	A1+
PPTFC	AA	-

L.T ENTITY RATING HISTORY



FINANCIAL DATA

PKR (mln)

	Jun-10*	Dec-09	Dec-08
Total Assets	16,923	16,416	12,172
Equity	6,724	6,525	7,253
Net Income	199	(728)	112
ROA %	2.4	(5.1)	0.7
ROE %	6.0	(10.6)	1.6
Equity / Assets (%)	39.7	39.8	59.6
SBP CAR %	34.2	37.0	57.0

** Based on unaudited accounts for 6 months ended June 30, 2010.*

ANALYSTS

Awais Z. Khan
+92 42 5869504
awais@pacra.com

Adnan Dilawar
+92 42 5869504
adnan@pacra.com

TFC Issue:

PHLC is in the process of issuing a secured, Privately Placed Term Finance Certificate (PPTFC) of PKR 1,000mln (inclusive of a green shoe option of PKR 250mln) for five years tenor. The instrument would be repaid after a grace period of two years in six equal semi-annual installments commencing from 30th month from the issue date. The profit is payable at 6 month KIBOR plus 160bps semi-annually in arrears. The instrument would be secured by a Fixed Charge over loan and lease receivable of PLHC with 25% margin. The instrument has a call option, which can be exercised after 12 months of the issue date by providing a 60 days notice to the trustee.

RATING RATIONALE AND KEY RATING DRIVERS

- The ratings reflect the sovereign ownership structure of PakLibya Holding, jointly owned by the Governments of Pakistan and Libya, signifying strong financial support. The ratings factor in the company's recent initiatives of fortifying its system and controls and management structure, which are expected to benefit its prospects. Meanwhile, performance of the company remains relatively constrained. Although a detailed business plan has been formulated, the efficacy of the plan, in terms of tangible outcomes in prevailing tough operating environment, remains to be seen.
- The management's ability to successfully implement its strategy in a timely manner, while managing the associated risks, would remain critical for the ratings. Moreover, maintaining strong asset quality and upholding high governance standards would be crucial.

ASSESSMENT

- The global financial crisis impacted the Pakistani economy with a lagged effect. Although certain macroeconomic indicators have improved, the chronic power crisis, stubborn inflationary pressure, and adverse law and order situation affected the overall economic activity and, in turn, the asset quality of the financial institutions. DFIs in Pakistan face many challenges in fulfilling their mandate including intense competition from commercial banks, limited outreach, and lack of viable funding sources. Thus, the sector relies heavily on money and capital market operations for generating profitable returns.
- Established in 1978, PLHC is one of the oldest DFI in the country and its core activities are divided into three main functions: i) Corporate and Investment Banking, ii) Treasury and Money Markets and iii) Securities Portfolio Management (SPM). CY09 proved to be a challenging year for PLHC as the company suffered losses largely emanating from significant provisioning expense for NPLs and diminishment in the equity investments. During 1HCY10, following its charter, PLHC is actively pursuing growth in loan disbursement as evident by expanding advances portfolio (1HCY10: PKR 7,885mln, CY09: PKR 6,717mln). The company continues to mobilize certificates of investment (CoIs), while reducing its borrowings from money market. PLHC's mark-up earnings witnessed increase, mainly attributable to higher quantum of business. During 1HCY10, PLHC reverted back to profitability on the back of substantial improvement in the capital market operations (1HCY10: PKR 57mln, 2009: PKR -613mln) and sizeable reduction in provisioning expenses (1HCY10: PKR -11mln, 2009: PKR 622mln).
- PLHC's investment portfolio comprises around 25% (CY09: 26%) of asset base as at end-June 2010. Equity investments constitute majority (42%) of the portfolio followed by government securities (26%), mutual funds (23%) and strategic investments (9%). The management is reconfiguring its equity investment portfolio by rationalizing number of scrips and focusing on high dividend yielding stocks of blue chips companies to optimize returns while reducing market risks.
- Owing to a sizeable advances book (PKR 10,917mln, including TFCs & Sukuks), PLHC's credit exposure remains high. The majority of PLHC's loans are long-term financing lines directed towards corporates within three sectors; power, chemical & pharmaceuticals and telecommunication representing around 55% of the credit portfolio. PLHC's top twenty funded exposures remain high (1HCY10: 83%, CY09: 88%) and thus, exposes PLHC to concentration risk. Delinquencies in loan book improved marginally and stood at around 9% in 1HCY10 (CY10: 10%) emanating almost entirely from corporate portfolio. Moreover, PLHC's advances portfolio is not expected to be materially impacted by recent floods as it has a very limited exposure in flood affected areas. Nevertheless, with subdued economic environment, maintaining strong asset quality would remain a challenge for the company. In this regard, the company has engaged external consultants to update its various policies and procedures pertaining to credit, market, liquidity and operational risks. Meanwhile, the organizational structure and risk management function have been streamlined to align with envisaged business growth plan.
- Going forward, the management has adopted a five-year business plan that entails a multi pronged strategy. The company would focus on its core activity – project financing – to establish sustainable revenue stream, while money market and capital market operations would supplement the profitability. The management also intends to elevate PLHC to a holding company structure by establishing entities or formulating strategic partnerships in promising sectors of the economy including banking, shipping, sugar, power, real estate and fertilizer. On the liabilities side, the main focus would be on rationalizing cost of funds while generating longer tenure funding base through financial intuitions and by issuing TFCs/ Bonds. Meanwhile, as per Government's plan to focus on building infrastructure, PLHC would be participating in long-term infrastructure bonds as and when launched.
- PLHC generates funds through CoIs and money market borrowings, which are largely short-term in nature. In order to effectively match its maturity profile, PLHC is issuing a PPTFC of PKR 1,000mln. The capital structure of PLHC primarily constitutes Tier I Capital and remains strong. However, it is on the lower side when compared to peers.

PROFILE

- PLHC, established as a joint stock company in 1978, is equally owned by the Government of Pakistan and the Socialist Peoples Libyan Arab Jamahiriya, through SBP and LFICO, respectively. LFICO, a state owned company, has a large portfolio of investments spread over Africa, Asia, Europe, and Americas.
- The six-member board of PLHC has equal representation of both sponsor countries. The Chairman, General Ehsan Ul Haq (Retd) is a Pakistani national; however, the Libyan Government has nominated him. Mr. Kamaluddin Khan, the managing director of the company, has extensive experience in the financial sector, both local and international. A senior management team consisting of seasoned bankers, whom have shown a high stability and loyalty over the years, assists him.