



## Rating Action

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## PACRA SEES CONCERNS FOR INVESTMENT BANKING AND LEASING BUSINESSES

Investment banks and leasing companies, a segment of Non Banking Finance industry, play a crucial role in the overall financial structure of Pakistan. The sector, besides broadening access to financial services, encourages and enhances the investment and saving options in the economy. The sector has experienced a significant transformation and consolidation since the implementation of Non Banking Finance Companies rules in 2003, under which amongst other factors their risk management framework and equity base are strengthened.

In terms of business prospects, the sector faces stiff competition from commercial banks, which also offer homogeneous products and services at relatively competitive prices. However, lately various broad socio-economic risks including widening fiscal deficit, slowing GDP growth, rising inflation, squeezing foreign reserves, depreciating Pak rupee, and worsening law and order situation have significantly amplified the challenges for the sector. These negative developments, while provoking a general downturn in the whole economy, have brought liquidity crunch in the overall financial industry.

Investment banks and leasing companies have limited direct access to depositors and are heavily relying on bank borrowings/money market short-term funding. In current environment, where banks are facing liquidity squeeze, the borrowing lines for this sector has been curtailed making the liquidity management difficult. At the same time, the financing cost of roll overs has also gone up. Adding to the problems, the melt down and recent freezing of the stock market, while negatively impacting the earnings from this source, has put further pressure on the liquidity and cash flow position.

Meanwhile, given the prevailing economic turmoil, which has unexpectedly prolonged, it would be difficult for the sector to find new avenues for their targeted business expansion, at least over the near-term. Auto leasing/financing, which comprises the major part of overall leasing operations of this sector, halted because of declining purchasing power of consumers, mainly an outcome of high inflation and interest cost. Moreover, corporate sector is also affected by the rising interest rate scenario, and has put on hold most of the expansion plans, thereby reducing the demand for credit.

PACRA believes that performance of the investment banks and leasing companies could be weakened, going forward. Meanwhile, any significant deterioration in the asset quality may lead to a decline in their risk absorption capacity. However, the companies, having diversified product base alongwith long-term credit facilities available



to support their asset-liability management are expected to withstand their competitive positioning in the sector.

PACRA, as a part of its ongoing surveillance, is monitoring all developments very closely, and may take a client specific rating action wherever it is deemed appropriate.

We would like to emphasize that for any concern about the financial strength of a rated entity in the country, it is appropriate to consult the respective rating agency before drawing any conclusion. This does not necessarily exclude any independent analysis or objective reservations about the rating opinion. Nevertheless, discussion with the respective rating agency could only help in developing a more informed view about the company.

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