



Holding Companies (HoldCos)

Sector Study



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Holding Companies

Global Overview

- Globally, Holding Company structures are well accepted and growing, especially in the developed economies. The concept of establishing Holding Companies to form corporate groups is increasing because of the many benefits that the structure offers. A few of them are mentioned in the adjacent diagram.
- In USA, a Holding Company is defined as the parent business entity, usually a Corporation or LLC, that does not manufacture anything, sell any products or services, or conduct any other business operations. Its purpose, as the name implies, is to hold the controlling stock or membership interests in other companies in order to form corporate groups.
- A classic example of a Holding Company is the Alphabet Inc. - An American multinational Conglomerate), that was created through restructuring of Google in October 2015, and became the parent company of Google and several former Google subsidiaries.
- Another example is the Berkshire Hathaway Inc. – An American multinational conglomerate). The company wholly owns a wide variety of big businesses, and also owns significant minority holdings in public companies such as The Coca-Cola Company, Bank of America, and Apple.



Holding Companies

Local Overview

- As per the Companies Act 2017, a holding Company is defined as “a company which is another company’s holding company if, but only if, that other company is its subsidiary” while a subsidiary is defined as “a company in which the Holding Company controls the composition of the Board or exercises or controls more than one-half of its voting securities either by itself or together with one or more of its subsidiary companies”.
- A holding company is also sometimes called an "umbrella" or parent company.
- PACRA’s definition of Holding Companies (also referred to as HoldCos) is broader and encompasses a greater range of entities, as compared to the definition of HoldCos laid out in the Companies Act, 2017.
- PACRA defines HoldCos as entities which are primarily involved in holding controlling and/or non-controlling stakes (equity participation) in other companies for the purpose of generating capital gains and/or dividend income. These stakes may be in group companies or outside the group. For the purpose of sector classification, PACRA takes into account only those HoldCos whose primary business is investment in equity and debt instruments, mainly of group companies. Such HoldCos that have operations of their own are classified in the respective sectors to which their operations pertain.
- As per SECP Group Companies Registration Regulations’08: “Group” means a holding company and its subsidiaries registered with the Commission” (i.e. SECP).

Investment Types

HoldCos can make investments in Equity, Debt or Other Instruments.

- An **equity investment** is funds invested in a company by purchasing shares of that company. These could be listed or unlisted.
- **Debt investment** are fixed return investments in which an investor lends money to a firm or project sponsor with the expectation that the borrower will pay back the investment with interest.
- **Other Investments** refer to all investments not classified in equity and debt instruments.



Holding Companies

Investment Strategies

- Broadly speaking, HoldCos can be classified into two categories on the basis of their underlying structure, **investment holding companies** and **operational holding companies**.
- Following are the various types of investment portfolios of HoldCos.

Core

The entities where the HoldCo has operational control and are essentially a part of the HoldCo or treated as a wholly owned subsidiary. Financial stress for core entities will have a significant effect on the HoldCo's credit profile. It is very unlikely that the HoldCo would decide to divest

Strategic

The entities where the HoldCo has operational control and are essentially a part of the HoldCo or treated as a wholly owned subsidiary. Financial stress for core entities will have a significant effect on the HoldCo's credit profile. It is very unlikely that the HoldCo would decide to divest

Trading

These comprise listed equity stakes held in other companies classified as 'Available for Sale' and/or 'Held for Trading'. These investments are least integrated and are held primarily with the intention of deriving trading income. The key risks involved here are liquidity and market risks.

Operational segment which are treated as core business. These are embedded in the legal structure of the entity, offering full ownership with complete operational control. Major resource allocation is involved in operations and the management of those operations. Financial stress on operations can create a significant drag on the overall credit profile.

Holding Companies

Snapshot

- Market size:** Unlike other Corporates, the size of the HoldCos is gauged by their Investment books, primarily because their main stream business is managing investment portfolio and earning returns on these investments. Such HoldCos (rated by PACRA) are 10 in number and have a total investment book of PKR~345bln as at End-Mar'21 (PKR~351bln as at End-Dec'20). A large portion of investments is dominated by equity stakes (~63%) which are classified into core, strategic and trading categories according to their nature. Around ~29% of the Investment book pertained to debt as at End-Mar'21 (CY20:29%) while around ~6% belonged to other investments (CY20:~13%).
- In terms of total assets, the market size stood at PKR~446bln as at End-Mar'21 (CY20:PKR~454bln). As an asset protection strategy, a parent corporation might structure itself as a HoldCo, while creating subsidiaries for each of its business lines.
- Players:** HoldCos generally have diverse investment portfolios depending upon their investment policy and are protected from losses accrued by subsidiaries. Many HoldCos have significant investments in tradable short term securities which fosters their liquidity profile.
- Recently, trend is increasing towards investment HoldCos as major business houses in Pakistan have established their investment Holding Companies, including Engro, Packages, DH Corp, TPL etc.

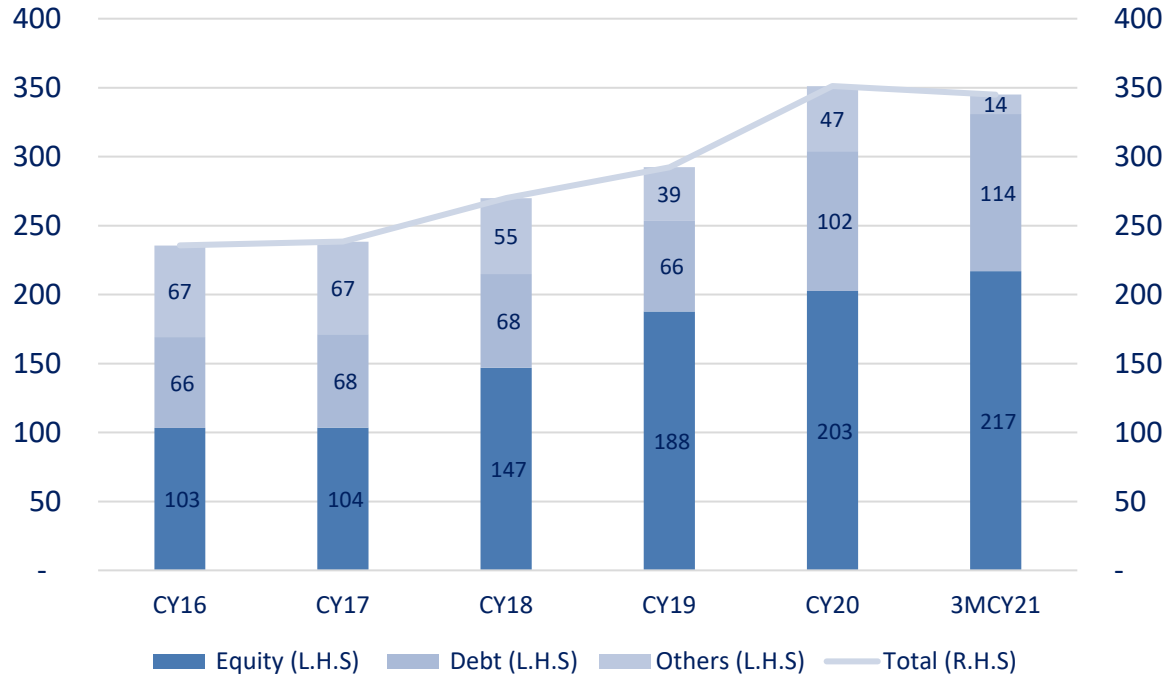
* Number of PACRA Rated clients

Industry Snapshot	CY19	CY20	3MCY21
Number of Players	10*		
Total Asset Size (PKR bln)	455	454	446
Investment Breakup (PKR bln)			
Total Investments	292	351	345
Equity Investments	188	203	217
Debt Investments	66	102	104
Others	38	46	24
Growth	8%	20%	-2%
Sector Structure	Organized and Listed (70% listed)		
Regulator	SECP		

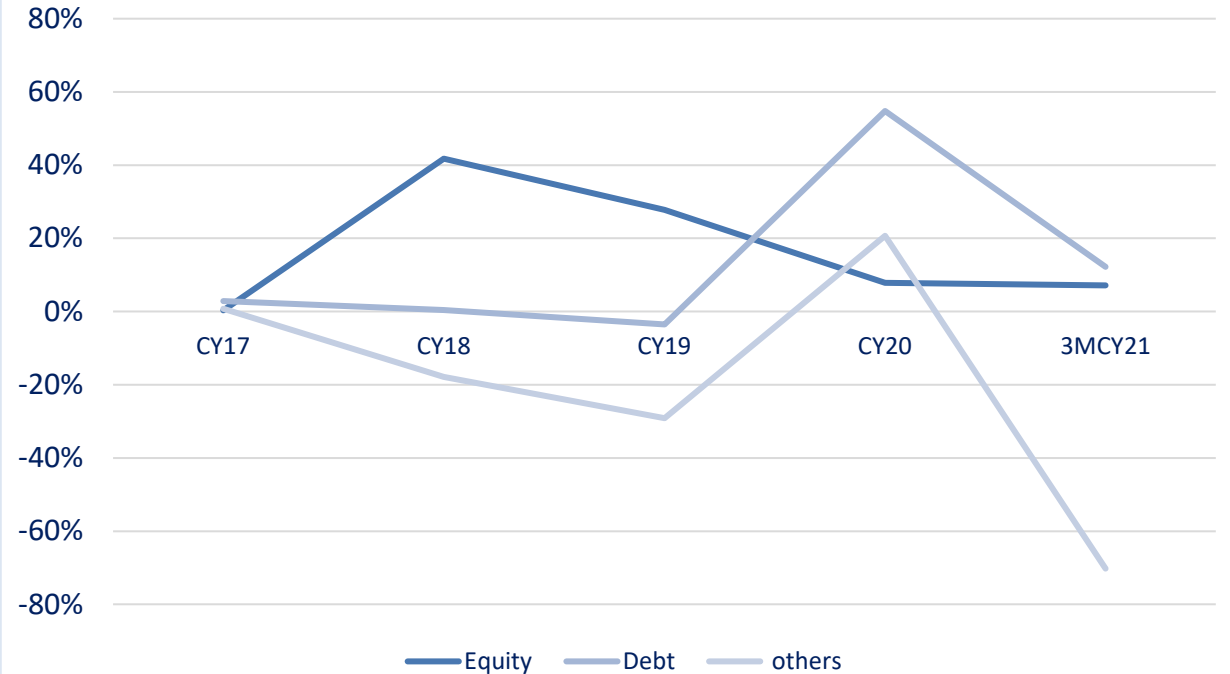
Holding Companies

Investment Portfolio

Break-up of Investments | PKR (bln)



Growth In Investments

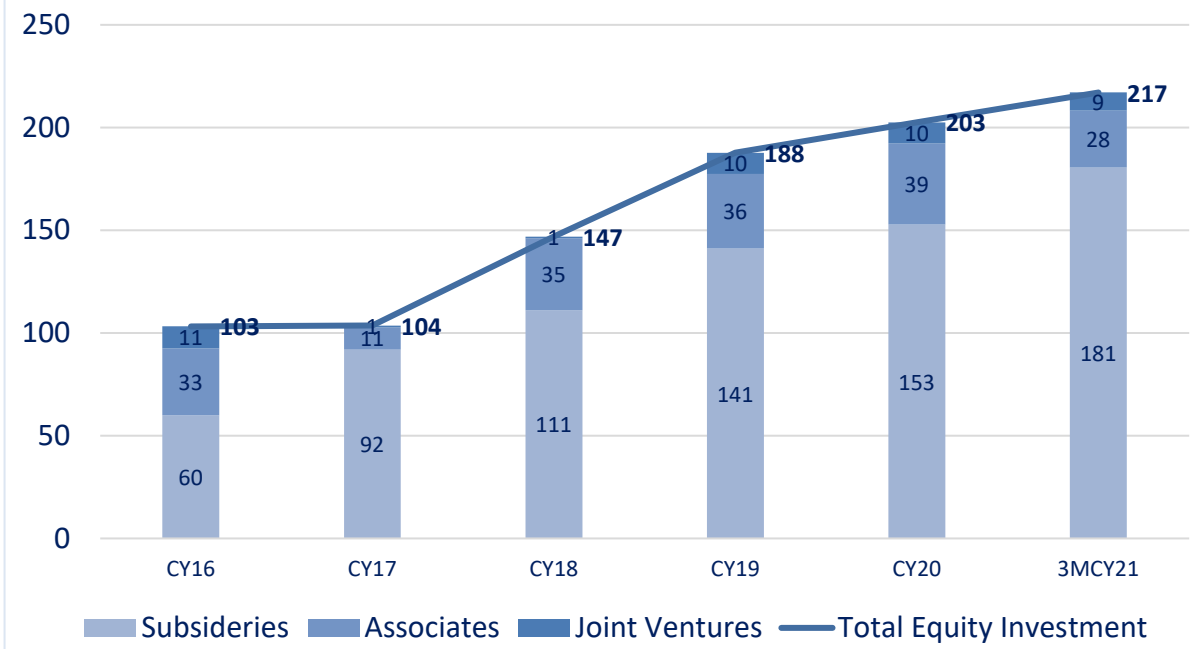


- Total Investments of the sector stood at PKR~345bln as at End-Mar'21 (End-Dec'20:PKR~351bln). Equity investments continued to grow at~7% recording at PKR~217bln as at End-Mar'21 (End-Dec'20: PKR~203bln) while debt investments grew at ~12% clocking in at PKR~114bln (End-Dec'20: PKR~102bln). Other Investments, which make up a small portion of the Investment portfolio, dropped by ~70% as at End-Mar'21 to PKR~14bln (End-Dec'20: PKR~47bln).

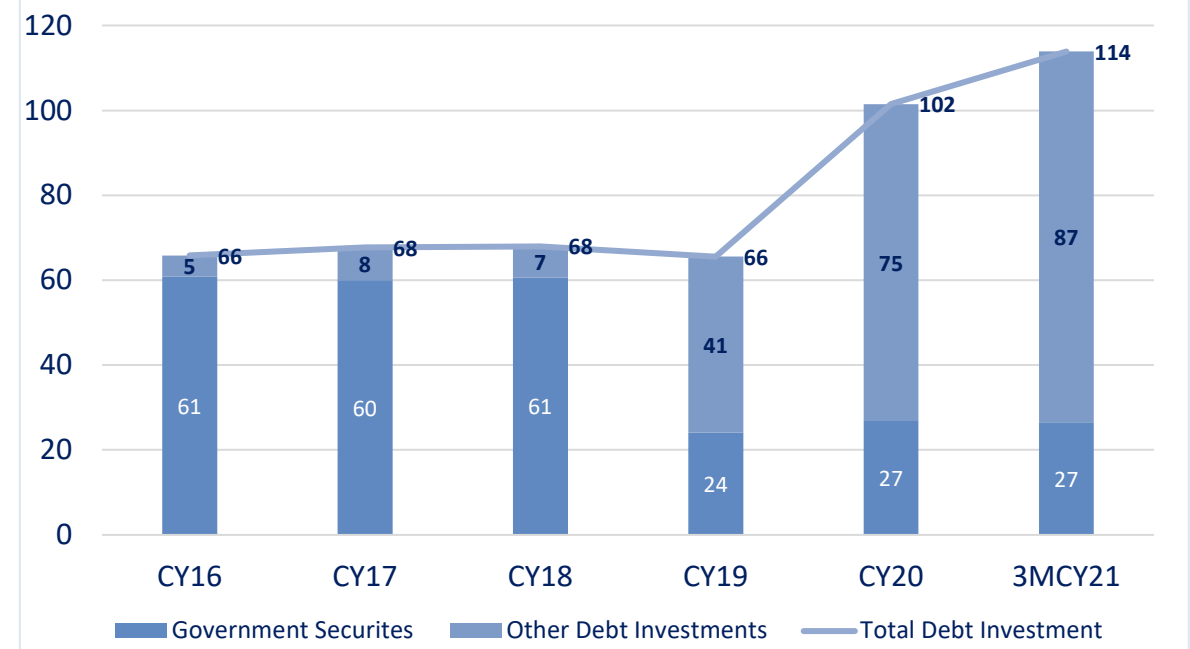
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Investments | Equity & Debt

Breakup of Equity Investment in PKR (bln)



Breakup of Debt Investments in PKR (bln)



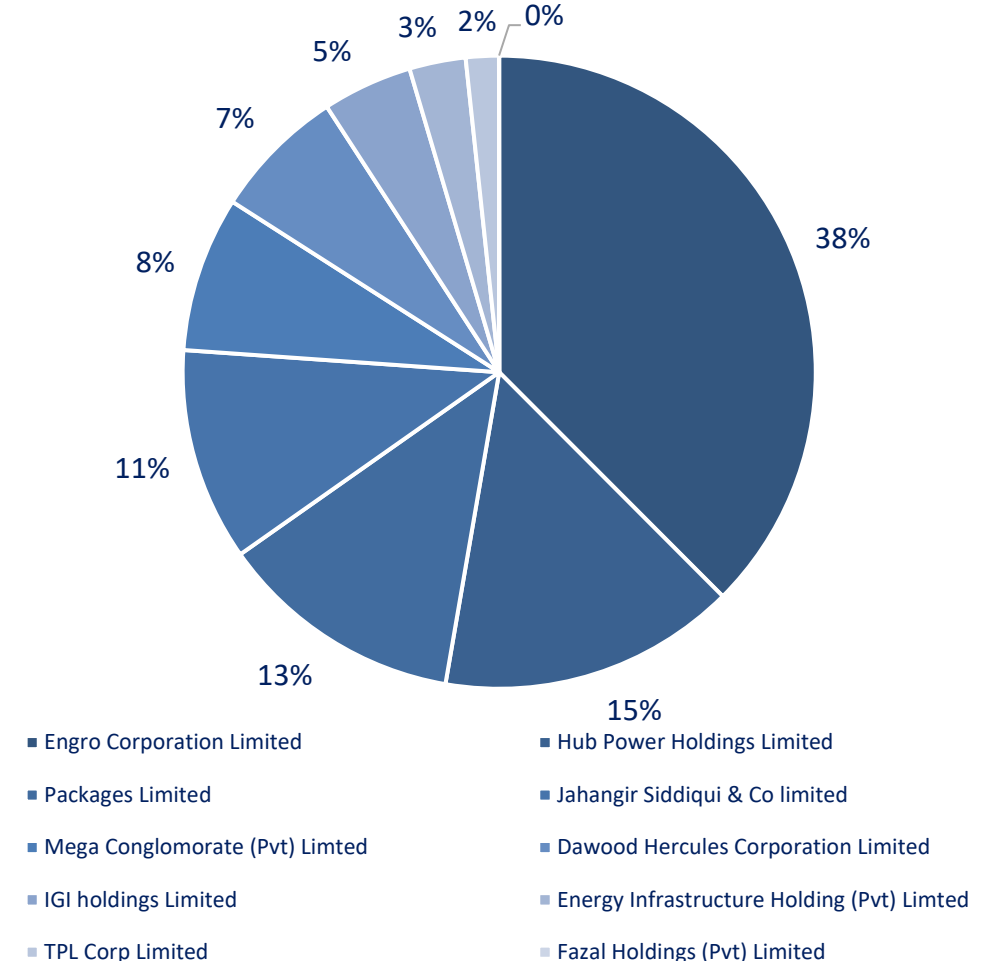
- Total equity Investments stood at PKR~217bln as at End-Mar'21 (End-Dec'20: PKR~203bln). Most of the HoldCos have strategic investments in subsidiaries (~78%) in which they have controlling interests and decision making powers. Only ~12% of equity investments are in associates and 4% are in joint ventures.
- HoldCos' debt Investment portfolio clocked in at PKR~114bln as at End-Mar'21 (End-Dec'20: PKR~102bln) which constitutes~23% Government Securities and ~77% other debt Investments.

Holding Companies

Investment – Company Wise

Total Investments	CY16	CY17	CY18	CY19	CY20
PKR bln	236	238	270	292	351
Engro Corporation Limited	37%	38%	35%	29%	34%
Hub Power Holdings Limited	2%	5%	8%	17%	16%
Packages Limited	21%	25%	19%	16%	13%
Jahangir Siddiqui & Co limited	13%	13%	10%	10%	10%
Mega Conglomerate (Pvt) Limited	1%	0%	9%	10%	8%
Dawood Hercules Corporation Limited	16%	10%	9%	8%	7%
IGI holdings Limited	6%	6%	5%	5%	5%
Energy Infrastructure Holding (Pvt) Limited	1%	1%	1%	1%	5%
TPL Corp Limited	1%	1%	2%	2%	1%
Fazal Holdings (Pvt) Limited	2%	2%	2%	2%	2%

Company Wise Investment Share | End-Mar'21



- In terms of market share in investments, ECorp has the highest share in the sector recording at ~38% of the investment book as at End-Mar'21 (CY20: ~34%). It is followed by Hub Power Holdings (15% as at End-Mar'21 and ~16% in End-Dec'20).
- The size of the investment book of a HoldCo is a depiction of the size of the business conglomerate itself, since the Sector's investments are largely deployed in subsidiaries. ECorp has a diversified equity portfolio in fertilizers, chemicals, polymers and other prominent sectors.

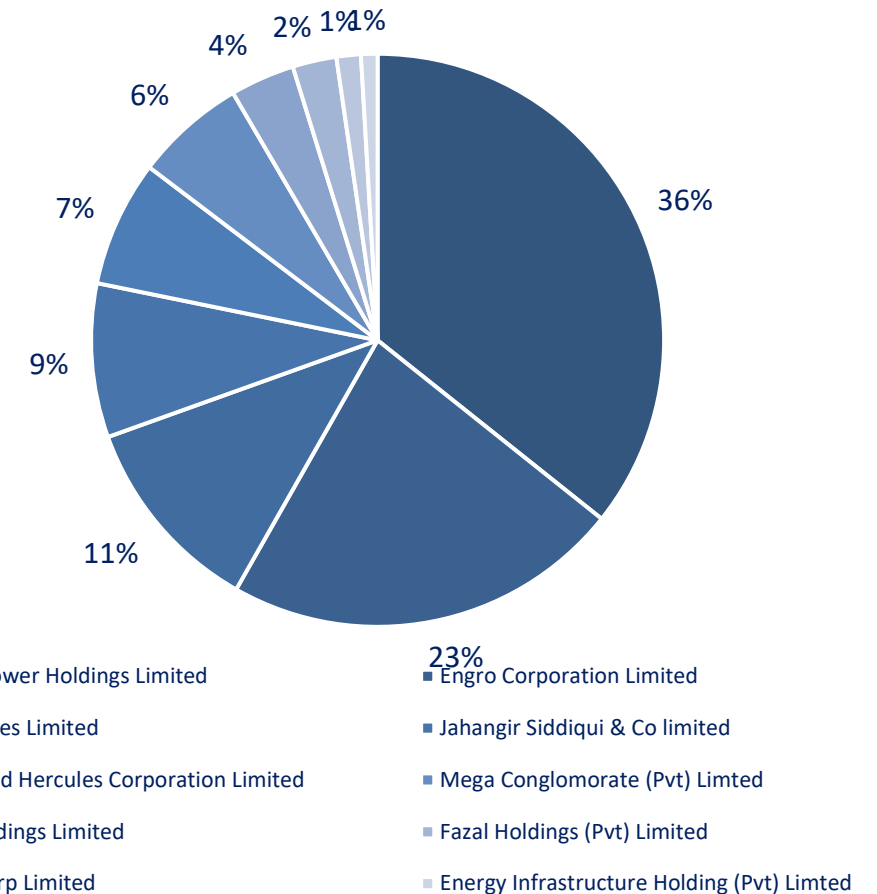
Holding Companies

Total Assets - Company Wise

Asset Size Company wise	CY16	CY17	CY18	CY19	CY20
PKR bln	395	406	417	454	453
Hub Power Holdings Limited	34%	34%	28%	34%	36%
Engro Corporation Limited	23%	22%	22%	21%	21%
Packages Limited	16%	18%	16%	15%	12%
Jahangir Siddiqui & Co limited	8%	8%	7%	6%	8%
Dawood Hercules Corporation Limited	10%	10%	11%	9%	9%
Mega Conglomerate (Pvt) Limited	0%	0%	7%	7%	6%
IGI holdings Limited	5%	4%	4%	4%	4%
Fazal Holdings (Pvt) Limited	2%	2%	3%	2%	2%
TPL Corp Limited	1%	2%	1%	1%	1%
Energy Infrastructure Holding (Pvt) Limited	1%	1%	1%	1%	1%

- Total assets of the Sector stood at PKR~445bln as at End-Mar'21 (End-Dec'20: PKR~453bln). This reflects that a major portion of the Sector's assets is deployed in its investments, with a small share of other operating assets. Almost ~36% of the Sector's assets belong to Hub Power Holdings Limited with ECorp being the next at ~23%, while ~ 11% belong to Packages Limited.

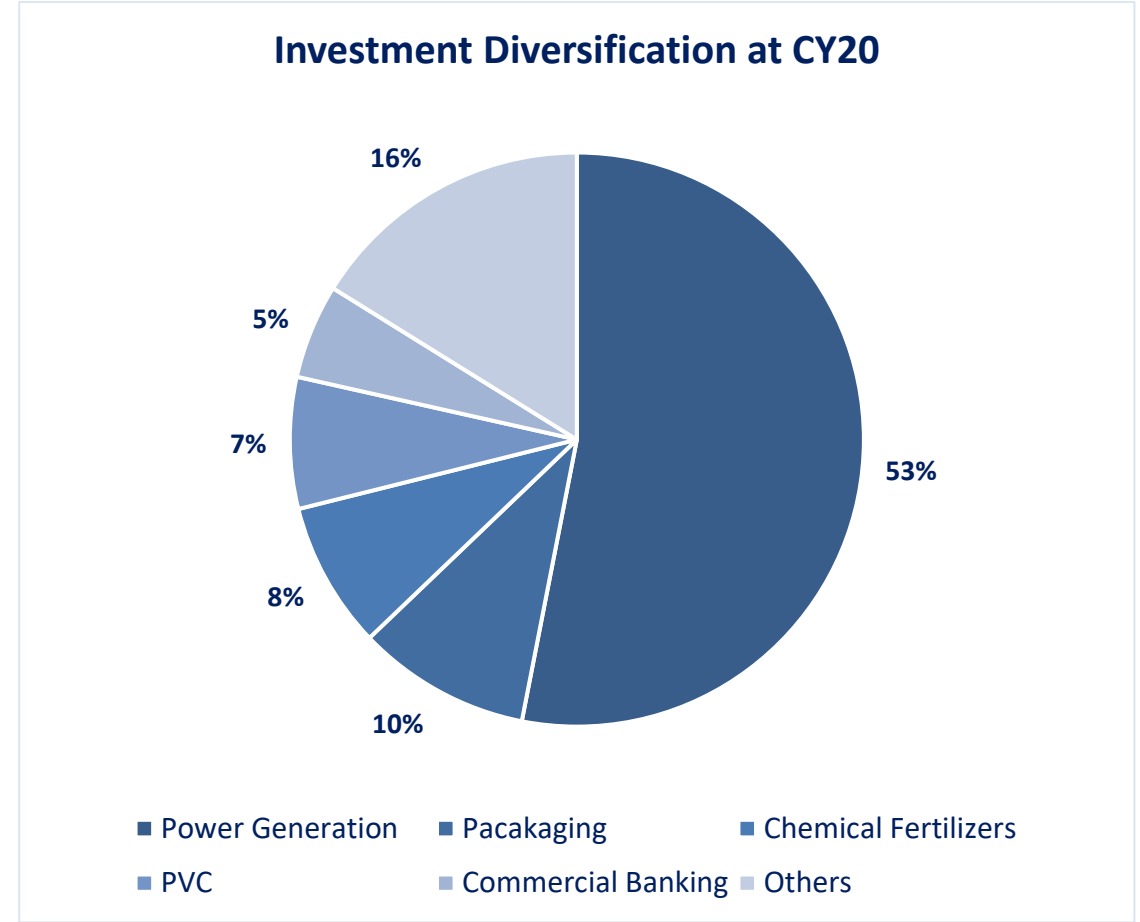
Company Wise Assets as at End-Mar'21



Holding Companies

Business Risk | Investment Diversification

- The business risk of HoldCos is correlated to the performance of their investments. The performance of investments can be evaluated in a number of ways, however, the key two factors used to determine the investment quality (covered in this report) are **‘diversification’** and **‘portfolio assessment’**.
- Measuring diversification of the Investments helps in evaluating the level of concentration the HoldCo possesses in a particular sector. The higher the diversification, the lower the risk and vice versa.
- Considering the Portfolios of top 5 listed players of the Sector (which account for ~84% of the Sector’s investments), the concentration of the Sector’s investments reflects elevation in power generation sector (53%). Others includes the investments in sectors, which are below 5%.

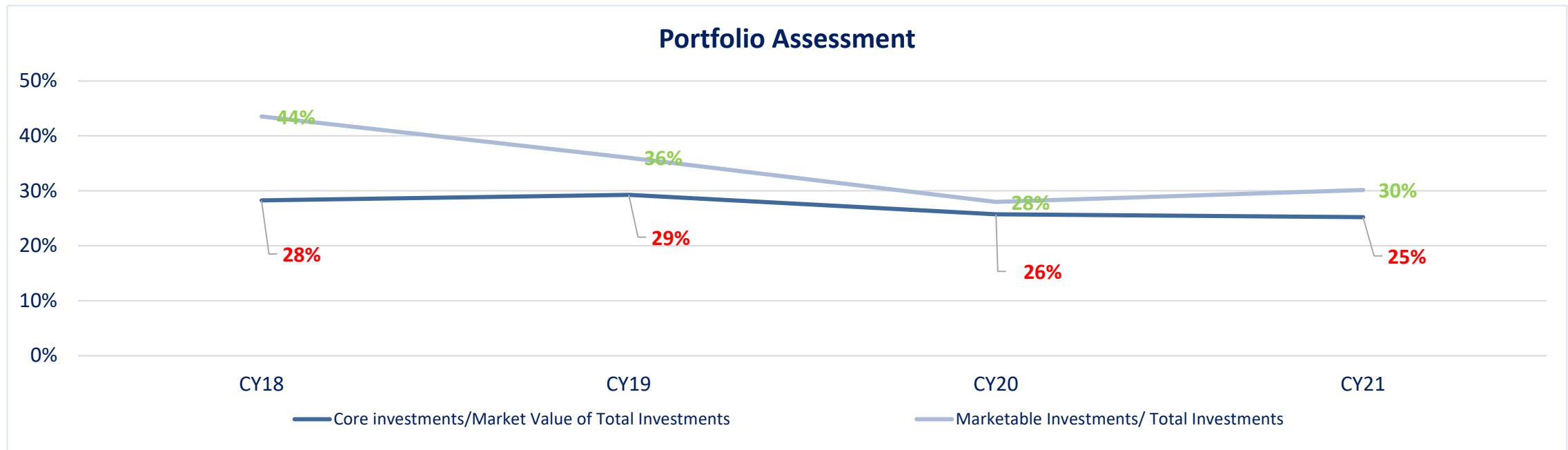


*Figures are estimated upon PACRA rated clients

Holding Companies

Business Risk | Portfolio Assessment

- Portfolio Assessment takes into account two key factors: (i) the level of core and marketable investments that HoldCos possess against their total investments at fair value. As per PACRA methodology, core investments are those where the HoldCo has 100%/wholly owned stake in a company. This implies that the HoldCo is fully exposed to the risks associated with its core investments. On the other side, Marketable investments are those that can be converted to cash at a readily available price. Such investments are necessary to provide support to the HoldCo's liquidity profile.
- The sector's core investments accounted for only ~25% of the market value of its total investments as at End-Mar'21 (End-Dec'20: ~26%), while marketable investments accounted for ~30% of total investments as at End-Mar'21 (End-Dec'20: ~28%).

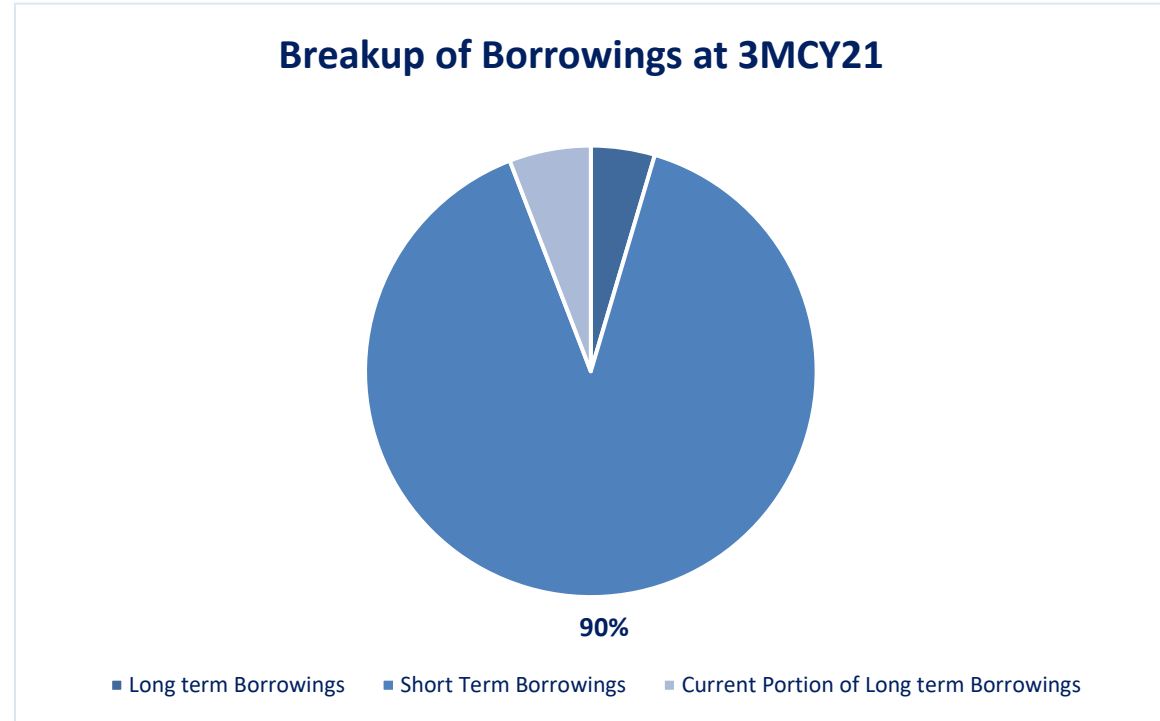
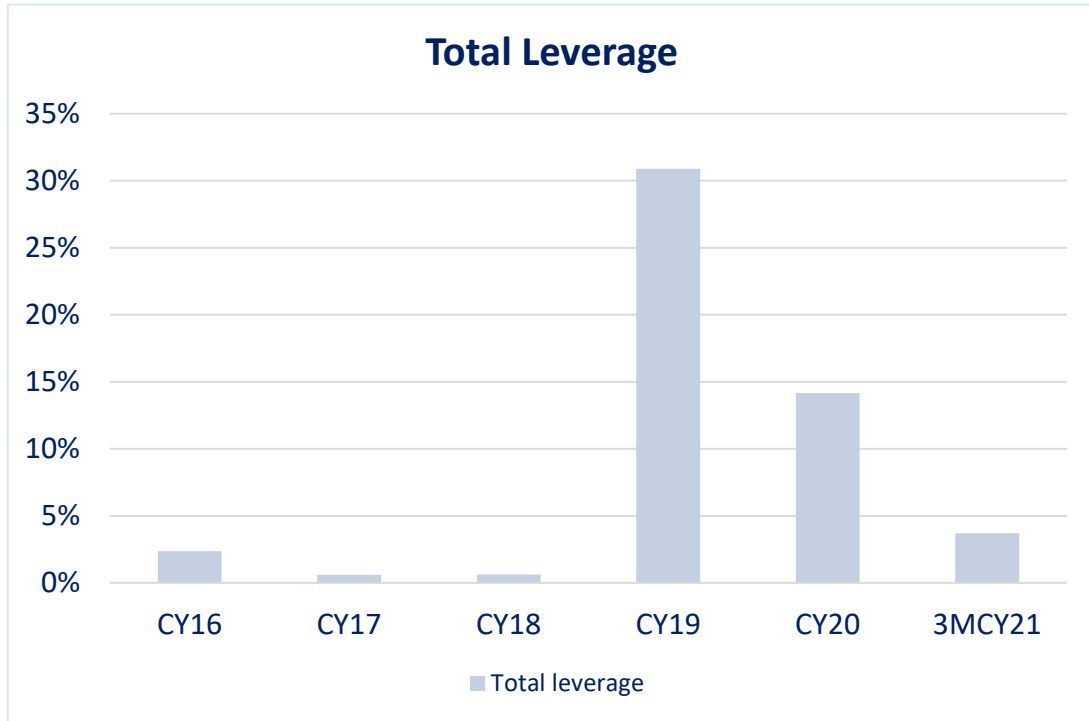


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Holding Companies

Financial Risk

- The leverage ratio of the sector has improved from ~14% to ~4% from End-Dec'20 to End-Mar'21, reflecting a robust internal capital generation. The borrowings comprise ~90% Short term borrowings (End-Dec'20: ~98%) and ~10% Long-term Borrowings (~2% as at End-Dec'20)
- In CY19, the short term borrowings increased to PKR ~46bln (CY18:PKR~26bln), due to issuance of debt instruments by a HoldCo in the power sector.

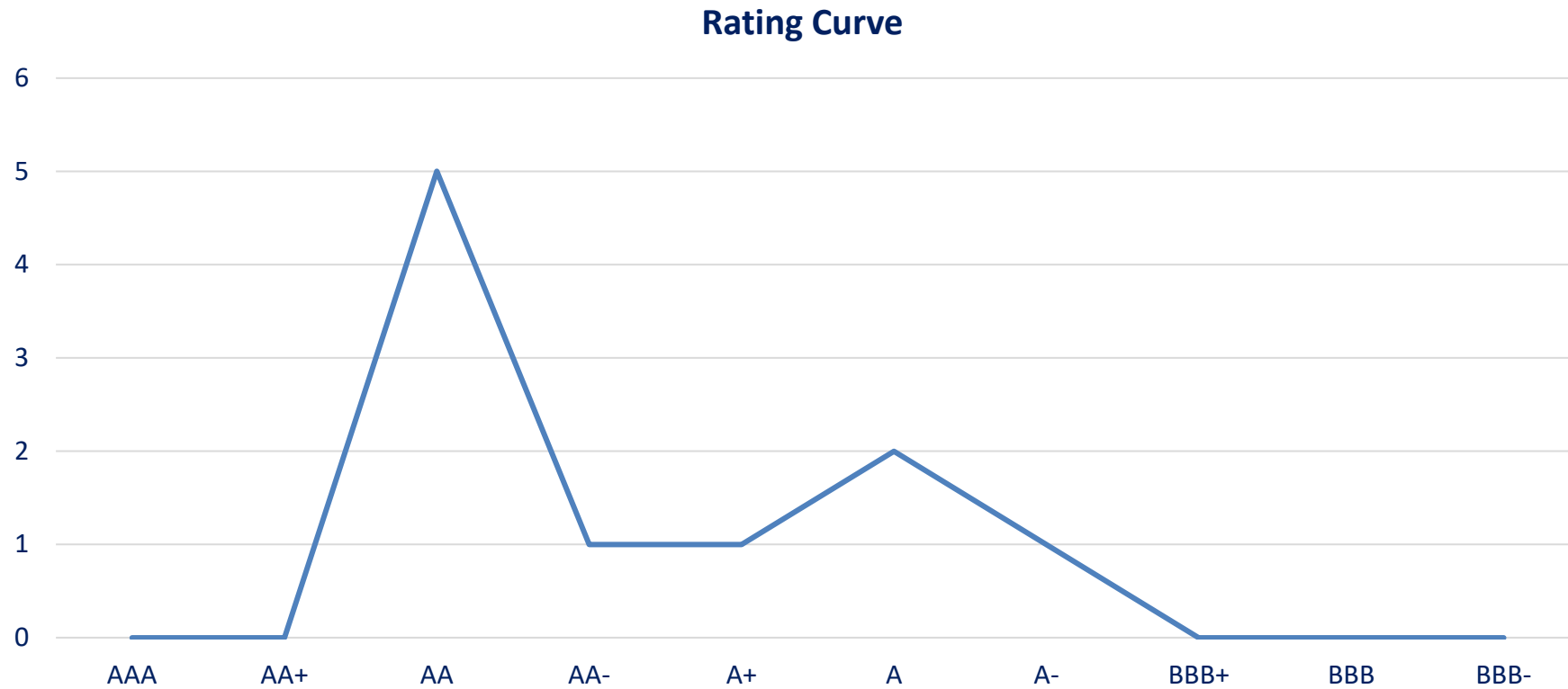


*Figures are estimated upon PACRA rated clients

Holding Companies

Rating Curve

- PACRA rates 10 clients in the Holding Companies sector.
- Rating Bandwidth of the sector ranges from AA to A- with 6 clients in the 'AA' category and 4 in 'A' category.



Holding Companies

Regulatory Framework

- The Securities and Exchange Commission of Pakistan (SECP) has implemented the Group Companies Registration Regulations, 2008 to provide a regulatory framework for the formation of group companies, comprising a holding companies and its subsidiaries.
- The Commission registers the holding company and its subsidiary companies as a Group in the prescribed form.
- The Commission is also empowered to cancel the registration of the group if any company within the group fails to comply with the requirements of the Regulations or any direction given by the Commission.
- After registration of the group, the HoldCo ensures that the group is in compliance with the requirements of the Code of Corporate Governance, International Financial Reporting Standards as applicable in Pakistan, and that transactions by any company within the Group with its associated companies and associated undertakings are carried out and recorded on an arm's length basis.
- The Regulations also facilitate streamlining of the group ownership structures and consolidation of the present complicated cross-company ownership to make the corporate sector internationally competitive.
- **Budget FY22:** Surrender of tax losses between eligible group companies has been allowed since 2007. The provisions allow both holding and a subsidiary company within the group to surrender their respective losses. An editorial amendment has been made to remove the ambiguity for surrender of losses by the holding companies.

Holding Companies

SWOT



Outlook: Stable

- The trend of establishing HoldCos to manage group structures is gradually increasing, as is witnessed in most of the big business groups such as Ecorp, DHCorp, Packages, JS & Co. IGI, etc.
- The Sector is significantly organized with ~70% listing penetration of PACRA Rated HoldCos.
- Overall, the Sector has a sizable asset base and Investment book, clocking in at PKR~446bln and PKR~354bln respectively, as at End-Mar'21.
- The Sector's equity investment portfolio is majorly tilted towards the power sector (~53%), however, the remaining portfolio is well diversified in other sectors. Moreover, most of the HoldCos have a sufficient level of marketable securities in their investment book which provides support to their liquidity profiles.
- The Sector has a robust capital formation and equity base to meet the financial needs of its subsidiaries and other strategic investments.
- Overall, the trend of establishing HoldCos structure is expected to increase, going forward, since most of the country's large business groups have investments in a multiple number of companies operating in different sectors. This necessitates the need to establish a HoldCo structure for better management, control, financial discipline and synergies across the group.

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