



## Rating Action

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## PACRA REVISES LONG TERM RATING OF SME BANK LIMITED

The Pakistan Credit Rating Agency Limited (PACRA) has revised the long-term entity rating of SME Bank Limited (SMEBL) to **"B"** (Single B) [Previous: 'BB'], while short-term rating is maintained at **"B"** (Single B). The ratings indicate that capacity for timely payment of financial commitments is more susceptible to adverse changes in business and financial conditions. A **"negative outlook"** has been assigned to the ratings as well.

The ratings capture continuous erosion in SME Bank's equity, thereby weakening its risk absorption capacity. The bank is experiencing persistent delays in injection of fresh equity by the Government of Pakistan, the majority shareholder. The government has been allocating money for SMEBL in the annual budget for last many years, though decreasing it gradually; no capital injection has been made. Notably, no amount has been allocated in the latest budget (Budget-FY13: PKR 2,000mln; FY15: PKR 500mln; FY16: PKR Nil). Given recurring losses, the bank's business profile has deteriorated. Further delay in fresh capital injection may lead to complete equity erosion in CY16. These trends create doubts over recovery in business prospects of the bank.

Though management of the bank managed to reduce losses of the bank but given ongoing losses and deterioration in equity base, strong support from GoP is critical for bank's survival. The clarity of GoP on the role that SMEBL should play would facilitate in developing a comprehensive business plan. The plan, among other things, must elicit timely and sufficient injection of fresh capital or measures of efficiency in the bank's privatization, while identifying key milestones to be achieved by the bank for self-sustainability.

**The Bank:** SME Bank Limited (SMEBL) was incorporated in January 2002 as a result of amalgamation amongst certain developmental institutions - Regional Development Finance Corporation (RDFC) and Small Business Finance Corporation (SBFC) - of the government. The bank commenced commercial banking operations in May 2005. It operates a network of 13 branches. The Privatization Commission has approved to appoint a consortium of financial adviser for the privatization of SMEBL.

SMEBL is ~94% owned by Federal Government through Ministry of Finance (MoF), while remaining 6% stake is held by commercial banks. The overall control of SMEBL lies with government nominated seven-member Board of Directors (BoD). Currently, the positions of Chairman and an Independent Director are vacant. The CEO, Mr. Ihsan ul Haq Khan, assumed the role in Jun-14 and has prior experience in banking and finance.

## Applicable Criteria and Related Research

- Banking Sector - Viewpoint | Dec-15
- Bank Rating Methodology

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