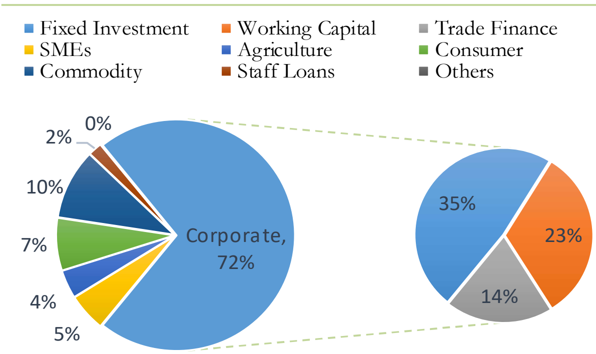
Chapter 6: The Corporate Sector

The overall performance and standing of non-financial corporate sector remained positive in CY20 though the ongoing pandemic posed significant challenges in terms of operating environment and supply chain constraints. A sample of top-100 listed firms witnessed improvements in their profitability, liquidity and solvency indicators while sales and business turnover indicators slackened due to weakened demand. Disaggregated analysis highlighted that automobiles, energy and oil & petroleum sectors faced notable contractions in sales. The investors' perception about the corporate sector oscillated with the outbreak of pandemic but confidence was restored by the year-end. Besides, the probability of default of selected firms slightly subsided and its levels in general remained on the lower side. The concerted efforts of the policy makers, however, may further improve the environment related to ease of doing business. Going forward, the dynamics of the ongoing COVID-19 pandemic and both coverage and effectiveness of vaccination drive will be the strong determinants of the corporate sector's performance.

Strong relationship between the corporate sector and the banking sector continues…

Banking sector remains the major financier of non-financial corporate sector of the country as the depth and outreach of capital market remains on the lower side. Amidst the pandemic, the interconnectedness between the corporate and the banking sectors further deepened as 71.58 percent (PKR 6.08 trillion) of the banks' domestic loan portfolio at the end of CY20 constituted non-financial corporations (**Chart 6.1**). Therefore, adverse shock in any of the economic sectors, which has significant borrowing from banks, can adversely affect the operating performance and solvency of the banking sector. Even deterioration in a sector, which otherwise is not a major borrower, can affect the overall economy due to its various linkages and may create stability issues for the banking sector.

Chart 6.1: Segment wise distribution of domestic advances, as of end December 2020



Source: SBP

As per the prevailing market practices, only the financial statements of the listed entities were publicly available, thus, this detailed assessment of the corporate sector's financial soundness and performance is based on the financial statements of selected top 100 listed non-financial firms representing companies from different economic sectors. In aggregate, these entities comprise 73.42 percent share in the asset base of all the listed companies. The listed companies have more formal and organized corporate governance structures and share their financials with external stakeholders and represent different sectors of the economy. The insights gained from the analysis of this sample firms presents a fair view of the standing and performance of overall corporate sector.

Despite pandemic, the overall performance of corporates recovered in CY20…

During the period under review, the pandemic posed a paramount health challenge across the globe. To curtail its impacts, almost all the nations introduced lockdowns, mobility restrictions measures and social-distancing protocols, bringing the world economic activity to a halt. As a result of these measures, supply-side issues spawned, cost of inputs surged and demand for goods and services sapped. Thus, the cash generation and debt servicing capacity of household and corporate sector endured significant pressure **(Chapter 1 and Chapter 3.1)**. Like most of the jurisdictions, the SBP introduced a host of measures to mitigate adverse impact on economic activity and employment in the economy, facilitate the liquidity of the borrowers and support the flow of bank credit and liquidity in the market.[178] Such support measures acted as the cushion to absorb downsides of the pandemic.

There was deceleration in the growth of corporate sector's assets (8.82 percent growth in CY20 against 12.41 percent in CY19) and domestic sales went down by 0.08 percent **(Table 6.1)**[179]. However, owing to cut in interest rates and policy measures to support the long-term credit and investment, corporate sector long-term borrowings increased, though it reduced current portion of long-term loans due to deferment and rescheduling relief given by SBP.

Nevertheless, , the corporates were able to improve profits after tax, primarily, backed by cut in interest expenses, which particularly started to reduce in the latter part of the year, and efficiency in administrative expenses and cost of goods sold (COGS).[180] Improved profits coupled with SBP support measures eased the pressure on the debt repayment capacity of the firms and compensated for the weakened demand, which also reflects in lower asset turnover for CY20.

Moreover, the liquidity indicators (e.g. current ratio) improved due to short-term investments and reduction in short-term borrowings and liabilities. The increase in short-term investments and assets hints at the tendency of the firms to maintain higher liquidity in the face of economic uncertainties during the pandemic.

Overall, the assessment indicated preservation of financial soundness and stable operating performance by the top 100 corporates.

Performance of various sectors remained mixed…

A few sector-specific risks and probable threats were the highlight of CY20. Cement sector faced risk of price hikes for coal, which is a major input for cement industry. Energy and oil sectors confronted with the challenges associated with circular debt issues. Auto sector faced rise in competition and threat to profit margins as the international players entered the market. Textile sector faced the exchange rate risk due to rise in imports of cotton to fill in the gap created by declining local production of cotton.

While the investors' confidence remained intact…

Market sentiments mainly reflected the changing macro-financial dynamics as indicated by high volatility in KSE-100 index during the year **(See Chapter 2)**. As a result, by the end of CY20, the credit worthiness of firms stabilized as reflected in improved credit ratings of selected firms, while investors' confidence reflected in improved market-based indicators.[181]

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178 Besides the govt. various schemes and packages, State Bank of Pakistan cut the policy rate by 625 bps and allowed payment holiday on principal amount of loans, rationalized prudential standards for restructuring of pandemic-stricken loans, and introduced different concessionary refinance schemes e.g. temporary economic refinance facility, refinance facility to combat covid-19 for hospital etc., Rozgar scheme to preserve the employment.

179 For CY20, the detailed financial position and performance of the selected companies are based on their financial of September 2020 quarter. The data of earnings and expenditure was projected/annualized to arrive at annualized indicators of returns e.g. ROE, etc.

180 Interest expense makes up 18.8 percent share of after gross profit costs of the corporates including administrative expenses, interest, financial expenses and tax expenses.

181 Further, most firms fell under investment grades.

Table 6.1: Financial Statements of PSX Listed Companies and Ratio Analysis

	Q3 CY18	Q4 CY18	Q1 CY19	Q3 CY19	Q4 CY19	Q1 CY20	Q3 CY20	*growth YoY*
				PKR billions				
Balance Sheet								
Non-Current Assets	3,043	3,115	3,187	3,344	3,501	3,534	3,676	*9.9%*
Net Operating fixed assets	*2,372*	*2,413*	*2,491*	*2,591*	*2,722*	*2,751*	*2,814*	*8.6%*
Intangible assets	*165*	*162*	*160*	*160*	*172*	*171*	*166*	*3.8%*
Long term investments	*383*	*410*	*411*	*453*	*460*	*450*	*515*	*13.7%*
Other non-current assets	*124*	*130*	*125*	*141*	*147*	*162*	*181*	*28.3%*
Current Assets	3,350	3,438	3,534	3,754	3,866	4,041	4,048	*7.8%*
Cash & bank balance	*202*	*190*	*210*	*198*	*218*	*218*	*219*	*10.3%*
Inventories	*704*	*701*	*748*	*728*	*735*	*739*	*637*	*-12.5%*
Trade Debt / accounts receivables	*1,366*	*1,405*	*1,402*	*1,577*	*1,641*	*1,733*	*1,767*	*12.1%*
Short term loans and advances	*122*	*120*	*131*	*116*	*129*	*134*	*134*	*15.9%*
Short term investments	*202*	*208*	*200*	*182*	*165*	*189*	*328*	*79.6%*
Other current assets	*753*	*814*	*843*	*952*	*978*	*1,028*	*963*	*1.1%*
Total Assets	6,393	6,553	6,721	7,098	7,366	7,575	7,724	*8.8%*
Shareholders' Equity	3,032	3,032	3,118	3,211	3,290	3,309	3,497	*8.9%*
Issued, Subscribed & Paid up capita	*547*	*552*	*553*	*554*	*562*	*575*	*567*	*2.5%*
Reserves	*2,312*	*2,307*	*2,393*	*2,474*	*2,546*	*2,570*	*2,724*	*10.1%*
Surplus on revaluation of fixed assets	*174*	*174*	*172*	*183*	*182*	*164*	*206*	*12.1%*
Non-Current Liabilities	843	878	924	968	1,050	1,088	1,191	*23.1%*
Long term borrowings	*412*	*466*	*483*	*482*	*558*	*594*	*680*	*41.1%*
Subordinated loans / Sponsor's loans	*4*	*7*	*8*	*7*	*7*	*6*	*5*	*-18.5%*
Debentures/TFCs (bonds payable)	*2*	*1*	*1*	-	-	-	-	*0.0%*
Employees benefit obligations	*70*	*79*	*75*	*80*	*87*	*85*	*84*	*4.2%*
Other non-current liabilities	*355*	*325*	*357*	*398*	*399*	*403*	*422*	*5.8%*
Current Liabilities	2,518	2,642	2,679	2,919	3,026	3,178	3,036	*4.0%*
Trade credit & other accounts payab	*1,463*	*1,464*	*1,499*	*1,639*	*1,696*	*1,746*	*1,851*	*13.0%*
Short term Borrowings	*668*	*808*	*769*	*869*	*915*	*994*	*728*	*-16.2%*
Current portion of non-current liabilit	*166*	*170*	*176*	*167*	*181*	*164*	*164*	*-1.8%*
Other current liabilities	*221*	*200*	*235*	*245*	*235*	*274*	*292*	*19.4%*
Total Equity & Liabilities	6,393	6,553	6,721	7,098	7,366	7,575	7,724	*8.8%*
Income Statement								
Sales	1,523	1,561	1,439	1,525	1,566	1,365	1,523	*-0.1%*
Local sales (Net)	1,509	1,551	1,429	1,505	1,549	1,351	1,504	*-0.1%*
Export sales (Net)	14	9	10	19	17	14	19	*-1.1%*
Cost of sales	1,257	1,304	1,185	1,271	1,307	1,143	1,243	*-2.2%*
Gross profit / (loss)	266	257	253	254	259	223	280	*10.3%*
General, admin. & other expenses	167	181	101	104	122	101	101	*-2.8%*
Other income / (loss)	29	52	32	38	43	43	39	*2.6%*
EBIT	127	127	184	188	180	164	218	*16.0%*
Financial expenses	27	37	36	46	51	57	34	*-25.5%*
Profit / (loss) before taxation	101	90	149	142	129	107	184	*29.4%*
Tax expenses	48	41	43	43	50	38	46	*4.7%*
Profit / (loss) after tax	53	49	106	99	79	69	139	*40.2%*
Financial Ratios								
Gross Profit Margin (%)	17.46	16.44	17.62	16.65	16.53	16.30	18.38	
Net Proft Margin (%)	3.49	3.16	7.37	6.49	5.04	5.09	9.10	
Return on Equity (%)	7.02	6.51	13.60	12.32	9.59	8.39	15.86	
Return on Assets (%)	3.33	3.01	6.31	5.57	4.28	3.67	7.18	
Current Ratio (units)	1.33	1.30	1.32	1.29	1.28	1.27	1.33	
Asset Turnover (%)	95.31	95.26	85.63	85.93	85.04	72.09	78.90	
Capital to Total Assets(%)	60.61	59.68	60.14	58.87	58.92	58.05	60.70	
Debt Equity Ratio (units)	1.11	1.16	1.16	1.21	1.24	1.29	1.21	
Debt to Capital Employed (units)	0.87	0.90	0.89	0.93	0.94	0.97	0.90	
Interest Coverage Ratio (units)	4.80	3.42	5.18	4.11	3.53	2.88	6.40	
Financial Leverage (units)	2.11	2.16	2.16	2.21	2.24	2.29	2.21	

Source: SBP

*Data of 100 companies were used that represent 73% of total assets of all listed non-financial entites

Corporates managed their costs effectively in the wake of difficult operating environment…

The consolidated financial statements exhibited augmented profits, despite dip in both local sales and exports. However, the corporate firms benefited from the significant cut in interest rates. In addition, corporates managed to make a marked reduction in their administrative and general expenses along with lower COGS. This reduction in costs led to improvement in profit margins and bottom line, as the after-tax profit of the selected large firms for Q3CY20 was 40.20 percent higher than the corresponding quarter of last year and ROE improved to 15.86 percent. The higher earnings and EBIT further augmented the debt repayment capacity for these corporate firms to 6.40 times in Q3CY20 (from 4.11 times in Q3CY19).

Growth in assets base decelerated during the year …

The growth of the asset base of the corporate sector decelerated to 8.82 percent in CY20 compared with 12.41 percent growth in CY19. Primarily, the current assets caused the slowdown, as the firms needed lesser amount of working capital in the wake of the pandemic. Inventory levels dropped significantly due to demand and supply constraints as well as the efforts of the firms to optimize the use of inventory in the face of uncertainties.

On the other hand, long-term borrowings augmented owing to drop in interest rates and funds borrowed under refinance schemes to support the long-term investment. Whereas, short-term borrowings declined due to lesser demand for inventories, inputs, and possibly better management of working capital in times of crisis. This phenomenon also reflects in the marked acceleration in banking sector's domestic lending to corporate sector for fixed investments, and decline in working capital loans (**see Chapter 3.1**). However, trade credit and other account payables increased by 12.73 percent in CY20 (11.47 percent in CY19). Thus, corporates replaced short-term borrowings with trade debts and payables. This ability of the high-end corporates to shift the funding to interest-free trade credit also reflects their bargaining power in the supply chain of production process.

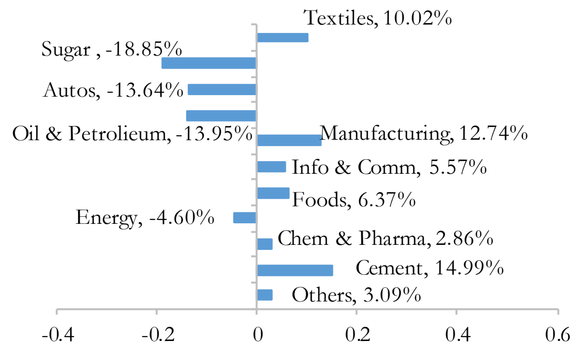
While the domestic focused firms witnessed decline in sales, the export-oriented ones benefited…

Prevailing pandemic worsened the macroeconomic dynamics, which adversely influenced the sales performance of the corporations during CY20. The total domestic sales in Q3CY20 were lower by 0.08 percent as compared to Q3CY19. During the first half of CY20, the domestic sales to fall by 5.14 percent. However, during Q3CY20 economic activities were restored with precautionary measures and various support measures started to mark their impact; accordingly, the output and sales started to recover. However, this recovery was not enough to make for the earlier hit during the first wave.

On the other hand, the alignment of exchange rate with market fundamentals increased the export competitiveness. Though, the pandemic-induced disruption in international trade was more severe the early resumption of business activities enabled the firms to capture the exports orders. Accordingly, the export demand made a quick recovery and exporters started to gear up their efforts to capitalize on this opportunity. However, because of the significant disruptions in supply chain and production process, the aggregate export sales of these firms for Q3CY20 were marginally (1.14 percent) lower than in the corresponding quarter of last year. However, detailed analysis and latest market information shows that the exports of these firms are following upward trend.

Chart 6.2: Sector-wise Sales Growth, CY20

(Percentages)



Source: SBP

The divergence in sales was quite visible among various economic sectors as well. Sugar, oil & petroleum, automobile and energy sectors experienced more stress. Together, they accounted for around 51.04 percent of the total corporate sector sales. On the contrary, firms in sectors like textiles, manufacturing, cement etc., which serve both domestic and foreign markets observed rise in sales **(Chart 6.2)**.

Debt repayment capacity improved towards the end of year and remained in comfortable zone…

Due to higher Earnings before Interest and Taxes (EBIT) and lower financing costs, the debt repayment capacity of the corporate sector started to improve markedly in the latter part of the year and remained in comfortable zone. The interest coverage ratio inched up from 4.11 in Q4CY19 to 6.40 in Q3CY20 **(Table 6.2)**. The solvency indicator, in terms of capital to total assets, appreciated marginally during the reviewed year, as the growth in capital levels was greater than rise in asset base. Accordingly, the debt equity ratio remained stable despite significant increase in long-term borrowings.

Table 6.2: Key Financial Indicators

	CY18	CY19	CY20
Profitability; Return on Equity (%)	7.02	12.32	15.86
Liquidity; Current Ratio (units)	1.33	1.29	1.33
Operational Effeceincy; Asset Turnover (%)	95.31	85.93	78.90
Solvency; Capital to Total Assets (%)	60.61	58.87	60.70
Leverage; Debt Equity Ratio (units)	1.11	1.21	1.21
Debt Repayment Capacity; Interest Coverage Ratio (units)	4.80	4.11	6.40

Source: SBP

Profitability improved due to enhancement in operating margin and reduction in financial costs and taxes…

The Return on Equity (**ROE**) of selected large firms increased from 12.32 percent in CY19 to 15.86 percent in CY20 **(Table 6.3)**. The Extended DuPont analysis revealed that improvement in operating profit margin partially absorbed the dampening impact of deterioration in the asset-usage efficiency, which deteriorated due to subdued sales. Moreover, decease in tax burden and financial costs led to the improvement in ROE.

Table 6.3: Extended DuPont Analysis

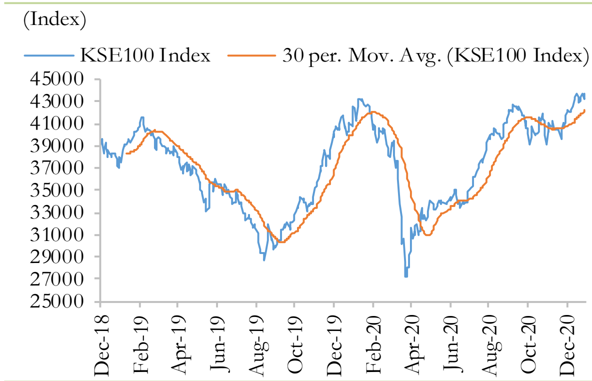
	CY18	CY19	CY20
Tax Burden (A)	0.53	0.69	0.75
Interest Burden (B)	0.79	0.76	0.84
Operating Profit Margin (C)	0.08	0.12	0.14
Asset Use Effeciency (D)	0.95	0.86	0.79
Financial Leverage (E)	2.11	2.21	2.21
Return on Equity (ROE) % (AxBxCxDxE)	**7.02**	**12.32**	**15.86**

Source: SBP

Market sentiments reflected the changing economic conditions…

KSE-100 index and its dynamics are used as proxy to gauge the market sentiments about the current and future performance of the corporate firms operating in Pakistan **(Chart 6.3)**. The CY20 commenced on a strong note witnessing approximately 41 percent recovery in the index from its low witnessed back in August 2019. At the end of February 2020, the pandemic surfaced in Pakistan and soon became a significant health and economic challenge for the nation. This slowdown also reflected in KSE-100 performance and the index lost 34.23 percent of its value in March 2020 compared with its level at the beginning of the year. Various economic support packages and relief measures helped the equity market to make V-shape recovery and the CY20 ended on the positive note with 60.70 percent increase in KSE-100 index from the lowest mark of March 2020. **(See Chapter 2)**.

Chart 6.3: KSE-100 Index



Source: PSX, SBP

Cement sector's overall performance and prospects turned positive by the end of CY20…

As the situation improved in Pakistan, the government allowed the resumption of construction activities quite early on. Moreover, the government announced incentive packages, which included, construction package, housing schemes and lower FED on cement. Cumulatively, these reforms have multiplied the gains for the cement sector entities in terms of local demand. Government policies focused on the construction sector and SBP's instruction to banks for allocating at least 5% of their domestic loan book for financing of housing and construction related projects positively contributed towards demand in cement sector.

On the export front, anti-dumping duty by South African authorities on exports from Pakistan were scheduled to end in the mid of December 2020.[182] While producers in South Africa are pursuing continuation of the imposed anti-dumping duties, in case these duties expire, it is expected to re-open a door for Pakistan cement exports. The exchange rate adjustment supported the price competitiveness of the sector; however, exports were only a nominal part of the aggregate cement sales during CY20. The outlook of the sector seems positive amidst the upbeat construction activities in the country. The hike in prices of inputs especially of coal could pose a threat to cement sector margins as it accounts for 40 to 50 percent of cost of goods sold, while increase in interest rates can also burden the bottom line of the sector.

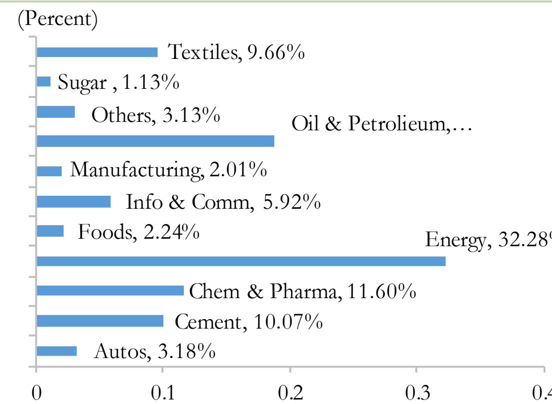
Power sector is likely to resolve trade debt…

Power sector continued to hold the major share of asset in corporate sector during CY20 among the sampled firms **(Chart 6.4)**. Though the operational performance of the power sector improved, it remained susceptible to the constraints posed by the rising circular debt.[183] The circular debt has reached PKR 2.33 trillion in CY20 (5.54 percent of GDP) starting from PKR 1.88 trillion by the end of CY19.[184] Increasing level of circular debt created liquidity crunch for the power sector entities and led to borrowing and additional financial costs.

To counter the liquidity issues, government and Independent Power Producers (**IPPs**) have signed MoUs to alter existing working arrangements (Power Purchase Agreements) and tariffs in order to reduce the burden of annual capacity payments and clear outstanding receivables of power producers. The government expects significant amount of savings in tariffs over the remaining life of these plants after these MoUs are converted into agreements. IPPs will benefit as they receive their outstanding trade debts.

While adjustments in electricity tariffs may help in curbing the buildup of circular debt, however, effective resolution of the issue require concerted efforts for curtailing the transmission and distribution losses.

Chart 6.4: Asset-wise break-up of sectors



Source: SBP

Oil & Gas sector remained under stress as well…

Oil & Gas is the leading sector in terms of both market capitalization as well as the quantum of borrowings from the banking sector. During the period under review, the local production of hydrocarbon failed to pick up despite the resurgence in oil demand and economic activity. Overall oil and gas production declined by 14 percent and 8 percent, respectively on year-on-year basis[185]. To counter the depleting reserves,

182 South Africa was used to be a major destination of cement dispatches. South Africa imposed anti-dumping duties on Pakistan based cement on Dec 2015 due to allegations of 'dumping' by Pakistani cement producers. Currently, they are under review by International Trade Administration Commission of South Africa (ITAC). However, the producers in South Africa are pursuing the authorities to extend the duties on Pakistan cement imports to secure their industry and impose duty on China and Vietnam imports of cement.

183 Rise in circular debt is due to recovery shortfall of electricity bills, structural issues in transmission and distribution network, delayed tariff adjustments and low usage of power plants.

184 Ministry of Energy, Power Division http://mowp.gov.pk/userfiles1/file/CircularDebtReport21.pdf

185 Optimus Capital Management, Market Strategy 2021

government has invited bids for 20 exploration blocks. It is anticipated that increase in exploration activity will help in enhancing the oil and gas production, and address the issues of depleting reserves.

Due to the closure of economic activities for few months in CY20, the petroleum sales witnessed overall decline in CY20. However, they registered improvement by the end of CY20 in sales figure. The recovery is mainly driven by uptick in passenger car sales, LSM growth and drop in international oil prices during the first half of CY20. High Speed Diesel (**HSD**) demand surged during the year due to government's efforts to curb the flow of smuggled cheaper Iranian products that drastically declined due to closure of border amidst pandemic and relaxation in transportation ban.

In CY20, government proposed new pricing mechanism of revising prices of Motor gas and HSD on a fortnightly basis in order to minimize the price volatility driven from exchange rate and international oil prices.

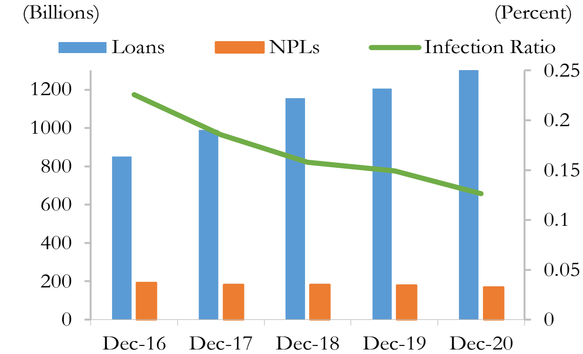
Textile sector enhanced their exports by the end of CY20…

Textile sector, being the major export-oriented sector, benefited most from the government's enabling policies, especially the subsidized utility tariffs, low interest rates and sales tax refunds. Besides higher credit offtake, the NPLs and infection ratio of the sector also witnessed declining trend **(Chart 6.5)**. Further, early easing in domestic lockdowns compared to regional countries and the US-China trade spat has enabled the sector to capture export orders and increase exports.

Given that domestic industry relies heavily on natural fiber whose local production is on the decline, the hike in the cotton prices, along with significant exchange rate appreciation against US dollar might hurt the profit margins of textile sector.

Nevertheless, new textile policy might play a pivotal role in improving exports and international competitiveness of the sector.[186] The policy includes subsidized borrowing rates, reduced power tariffs and support for SMEs.

Chart 6.5: Textile sector loans, NPLs and infection ratio



Source: SBP

Automobiles sector closed CY20 on a positive note in terms of sales volume…

Automobiles sector sales, which faced challenges during the first half of CY20 because of dwindling consumer demand, rebound in the second half. Among various supply-side and demand-side factors, auto financing remained the primary driver of increased demand and sales. Presently, auto financing comprises of approximately 35 to 45 percent of total auto sales.[187] Further, the prevailing low, single digit interest rate is expected to drive the sales volume and demand in positive direction.

Nevertheless, PKR depreciation led to massive hike in the vehicle prices over the last year that

[186] Textile and Apparel Policy 2020-25, it will replace previous 2014-19 policy. The new textile policy contains subsidies and lower tax rates. The electricity and gas tariffs will be consistent during the period of the policy. The objective of the policy is to boost exports for textiles and apparels.

[187] Next Capital, Pakistan Equity Market Strategy 2021

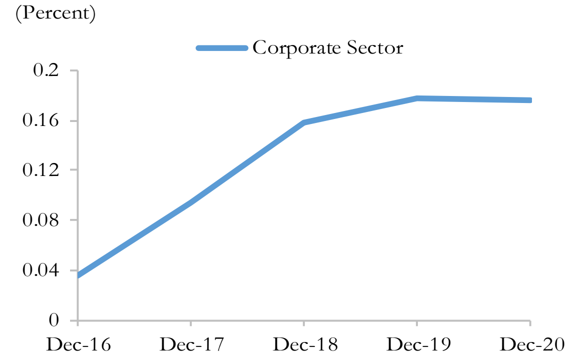
affected the demand. Further, supply chain issue originating from Asian ports has led to air shipping of parts, which involves higher input costs and cut in gross margins.[188]

Additionally, increase in competition due to new entrants, Kia, Hyundai, Changan and MG, and sanction of Electric Vehicles policy was expected to put downward pressure on the prices of vehicles. However, currency devaluation and changes in the interest rates remains important determinants of price and demand for vehicles and ensuing performance of the sector.

Probability of default for the corporate sector slightly declined …

The weighted average 1-year PD of selected firms of the corporate sector slightly declined to 0.176 percent in CY20 (0.178 percent in CY19) **(Chart 6.6)**.[189] The fall was primarily due to the general improvement in the overall performance and outlook for these firms, which was mainly enabled by timely government reforms and policies to support the economic activity. Improvements in operating performance of these firms increased investors' confidence—bolstered by successful recovery of macro-economic variables— and contributed to the fall in default probabilities. Further, the level of PDs, itself, is at the lower side and does not pose notable default risk to the lenders. As such, these corporate firms maintained strong financial soundness and decent operating performance despite challenging macro-financial conditions.

Chart 6.6: Weighted avg 1 year PD of Corporate Sector



Source: Bloomberg, SBP

Repayment behavior and financial standing of the leading borrowers remains strong…

A brief analysis of banking sector's top 30 borrowing firms indicates that banks seem to have higher exposures on large groups due to their better credit worthiness (**Box 6.1**). The COVID-19 pandemic and consequent lockdowns during CY20 raised significant challenges for borrowing firms in terms of operating environment and demand and supply constraints. However, due to early resumption of economic activity during latter half of CY20 and enabling support measures from central bank and government, the firms have largely weathered the impact of the pandemic.

Credit rating culture showed improvement…

In recent years, the rating culture among large firms has shown improvement, as firms tend to get themselves rated. During the reviewed year, this trend got further traction as the number of rated firms further increased: out of 314 non-financial listed entities, about 80.9 percent of them were rated in CY20 as against 77.17 percent in CY19.[190] However, in the universe of all registered public companies, the rated companies were merely 14.37 percent, which is still on the lower side. This is because many companies in Pakistan rely on

[188] The supply chains issues included shortage of shipping containers, hike in freight charges, delay in shipments and port congestion due to lockdowns in various countries around the globe.
[189]The PD (1 Year PD) is mainly driven by the quality of firm's liquidity management and ability to honor short-term obligations. The PD is calculated using Merton Model, which uses value of equity and volatility of equity to measure default probability.
[190] In CY19, out of 311 non-financial listed entities only 77.2 percent were rated.

indirect source of financing like banks or their internal sources (profit plough backs etc.) and rely less on capital market for their funding needs. Out of all the rated companies in the country, major chunk of the companies lies in investment grades (AAA to BBB-), which advocates high credit quality in terms of long-term ratings **(Table 6.4)**.

Table 6.4: Ratings of Companies in CY19 & CY20

Long-term			Short-term		
Ratings	**CY19 %**	**CY20 %**	**Ratings**	**CY19 %**	**CY20 %**
AAA	3.3%	3.1%	A1+	20.0%	20.1%
AA+	4.2%	4.3%	A1	26.3%	24.4%
AA	8.3%	9.1%	A2	40.0%	43.3%
AA-	7.5%	7.9%	A3	12.9%	11.4%
A+	7.5%	6.3%	Others	0.8%	0.8%
A	12.9%	13.0%			
A-	25.4%	26.0%			
BBB+	8.3%	8.3%			
BBB	10.4%	11.0%			
BBB-	5.8%	7.9%			
Others	6.3%	3.1%			

Source: PACRA, JCR-VIS

Whereas, in terms of short-term ratings, majority of the companies were rated as A2 that represent satisfactory capacity for timely repayment.[191] Companies rated in this category might be vulnerable to adverse changes in business, economic and financial conditions.

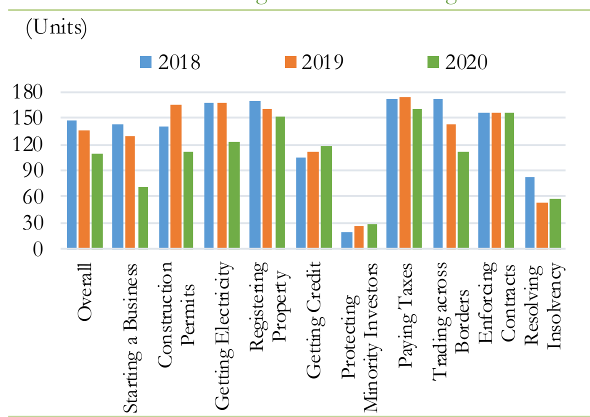
Ease of Doing Business ranking improved by 28 points…

Government of Pakistan has been making efforts to improve the ease of doing business. Over the last couple of years, there has been marked improvement in country's ranking on World Bank's "Ease of Doing Business" index. The country's ranking improved notably by 28 points from 136 to 108 on World Bank's Ease of Doing Business Index.[192] The score improved on account of getting electricity, trading across borders, construction permits and starting a business **(Chart 6.7)**.

Other areas where score improved included registering a property and paying taxes. Enhancement in the functionalities of the online one-stop shop by Government of Pakistan aided in starting a business segment. Furthermore, introduction of online payment of tax via internet banking, debit cards and Automated Teller Machines (ATMs) streamlined the tax payment process. Introduction of online mobile app further bolstered the filing of tax returns.

Moreover, integration of various agencies in the Web-Based One Customs (**WEBOC**) electronic system and processing of consignments through the Green Channel improved the score in the segment of trading across borders. Enhancement in the approval process and regular building quality inspections made procurement of construction permit relatively easier and safer. Additionally, the enforcement of service delivery time frames, launch of an online portal for new applicants and transparency in electricity tariffs enhanced the getting electricity segment.

Chart 6.7: Ease of Doing Business - Rankings



Source: World Bank, SBP

Improvements in the Doing Business rankings and establishing macroeconomic stability will send a

191 PACRA. (2020). Rating Scale. Pakistan, March. http://www.pacra.com.pk/uploads/doc_report/PACRA_Rating%20Scale_Corporate_FY18.pdf

192 World Bank. (2020). Doing Business 2020: Economy Profile Pakistan. Pakistan, March https://www.doingbusiness.org/content/dam/doingBusiness/country/p/pakistan/PAK.pdf

message to SMEs and large investors that Pakistan is open for business and will remain globally competitive. Furthermore, reforming regulations and procedures, improving ease of paying taxes and establishing an online business portal will improve the business environment in the country. Moreover, female entrepreneurship needs to be encouraged to establish business that will also aid in progressive formalization of the economy.

Outlook for the corporate sector rests on pandemic dynamics…

Due to the pandemic and dampened economic activities, the operating enviroment remained quite challenging for the corporate seector during the year under review. However, the corporate sector has successfully weathered these challenges and ultimately posted better operating performance. Going forward, the performance of the corporate sector will largely depend upon the dynamics of the pandemic, effectiveness of vaccination drive, and the associated impacts on macro economy.