

**FIRST FIDELITY LEASING MODARABA (FFLM)****RATINGS (MARCH 2007)****FIRST FIDELITY LEASING MODARABA**

	NEW	PREVIOUS
<b>ENTITY</b>		
Long Term	A-	A-
Short Term	A2	A2

**FINANCIAL DATA**

PKR (mln)

	30-Jun-0	30-Jun-05
Total Assets	577.47	662.07
Equity	317.07	315.65
Profit after Tax	27.83	24.02
ROA %	4.49	3.84
ROE %	8.80	7.58
Equity/Assets %	54.91	47.68

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**ASSESSMENT**

- The ratings reflect FFLM's sustained strong risk absorption capacity emanating from its pre-dominantly equity based capital structure and adequate asset quality. However, at the same time, the ratings factor in the Modaraba's low profitability and somewhat limited growth prospects in an increasingly growing and competitive financial sector.
- FFLM's performance has been subdued over the years, though showing a slight improvement during FY06. This was mainly because of overall increase in interest rates, leading to a direct improvement in spreads as there was no corresponding offsetting factor given the Modaraba's capital structure. Nevertheless, the Modaraba's high cost structure, along with its small size, kept its profitability lower than its peers. In line with the Modaraba's business philosophy to maintain low credit risk expansion, leasing activity was sluggish, resulting in reduced asset size. During the year, there was no other significant development that could signify material improvement in the Modaraba's prospects. Meanwhile, income from brokerage operations, which the management intended to divest previously, is expected to provide a relatively stable revenue stream, though contribution towards the total income would be modest.
- Going forward, the management's earlier strategy remains intact of focusing on property investments. Given the Modaraba's relatively limited risk management and overall control systems to support credit expansion, the management aims to gradually reduce the finances portfolio and instead, build up the property investment portfolio. On the longer run, FFLM would be entering into housing finance and real estate development activities. The business model envisages that housing finance would be linked to the development of the Modaraba's own projects. The timely execution of this plan is expected to support the Modaraba's profitability but in the increasingly competitive operating environment the extent of improvement may not be substantial.
- The asset quality remains adequate with minimal fresh infection in the recent period. The Modaraba is aggressively pursuing recoveries against a few of its chronic NPLs and any success in this regard, given full provisioning already made, would have positive impact on the bottom line. Meanwhile, the higher concentration in vehicle leasing – contributing above 67% towards the total leased assets – has positive connotations for asset quality, given the low default rates and relative ease of repossession and disposal.
- Given the management's conservative growth stance, the Modaraba does not maintain a large funding base. The limited operations are being supported largely by equity. Considering that the Modaraba is not envisaging any major growth, the gearing is unlikely to increase substantially.

**RATING OUTLOOK & KEY RATING DRIVERS**

- FFLM's performance continues to remain constrained due to the Modaraba's limited ability to generate a reasonable level of profitability. While in the sector a few peers have undertaken initiatives to tap growth opportunities through product innovation and identification of niche markets, FFLM's performance is likely to remain subdued. This is partly attributable to a pool of assets, which are not generating revenue. These assets continue to be held in anticipation of regulatory approvals that are expected to facilitate the implementation of management's strategy to focus on property development. Any further delay in the approval process could have negative implications.

**PROFILE**

- FFLM, listed on all the three stock exchanges of the country, was established in 1991 and is managed by Fidelity Capital Management (Pvt.) Limited. During FY05, Crescent Standard Business Management (Pvt.) Limited (CSBML) acquired the entire shareholding of the management company of the Modaraba. CSBML is a part of Crescent group and mainly serves as a holding company for the group's interest in various entities. The Crescent group is one of the well-known corporate groups in Pakistan with diverse interests.
- The board of directors of the management company comprises five members including chief executive officer. The CEO, a Chartered Accountant, has substantial experience in the financial sector. While the Modaraba operates principally from its head office in Lahore, it also has branches in Karachi and Islamabad.