



RATINGS (SEPTEMBER 2009)

FIRST FIDELITY LEASING  
MODARABA (FFLM)

ENTITY	NEW	PREVIOUS
Long Term	A-	A-
Short Term	A2	A2

A					
A-					
BBB+					
BBB					
	February 2005	April 2006	March 2007	April 2008	September 2009

FINANCIAL DATA

PKR (mln)

	31-Mar-09*	30-Jun-08
Total Assets	472.5	494.2
Equity	345.8	365.5
Profit after Tax	6.7	41.7
ROA %	1.8	8.2
ROE %	2.5	11.6
Equity /Assets %	73.2	73.9

\* Based on unaudited accounts for 9 months.

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RATING RATIONALE AND KEY RATING DRIVERS

- The ratings reflect FFLM's sound low leveraged capital structure supplemented by unrecognized gain on investment properties. Moreover, the Modaraba continues to have good asset quality, indicating prudent risk management. FFLM's growth, though recently has come under pressure mainly as a result of subdued operating environment, is expected to improve in tandem with the economic recovery.
- The ratings are dependent on the sustained competitiveness of the Modaraba in the increasingly tough environment. Meanwhile, any significant mismatch amongst asset and liability classes, resulting in liquidity and/or interest rate risks or any substantial deterioration in FFLM's asset quality could have negative implications for the ratings.

ASSESSMENT

- FFLM provides financing through three modes: *Ijarah*, *Morabaha*, and *Musharaka*. *Ijarah* – dominating the Modaraba's overall financing portfolio (42%) – comprises operating lease of plant & machinery, vehicles, and equipment. *Musharaka* – second in the portfolio mix (30%) – covers the real estate development project. The third financing medium – *Morabaha* arrangement (28%) – involves financing of different kind of goods.
- During FY08, though FFLM's finances portfolio declined on a YoY basis, its gross revenue increased substantially mainly attributable to better returns on *morabaha* financing due to asset reprising in line with rising interest rates. Financial charges witnessed a rise owing to both higher average borrowings and interest rates. Brokerage income declined as a result of sale of FFLM's seat in the Lahore Stock Exchange. Nonetheless, this helped FFLM to book a one time gain of PKR 33mln, resulting in higher reported profitability.
- During 3QFY09, FFLM continue to benefit from high interest rate environment of the country. Consequently, the Modaraba posted slightly higher net interest revenue on an annualized basis. However, due to marginal brokerage income and impairment loss of PKR 5mln, the profitability went down significantly on a comparative basis.
- Going forward, the management, while following a modest growth strategy, intends to expand its *ijarah* portfolio through further penetrating, though cautiously, into the existing sectors. Moreover, FFLM plans to diversify into the construction sector, mainly focusing on the *ijarah* of related machinery. This new revenue stream, with relatively high demand, is expected to provide better returns against the conventional auto *ijarah*. However, the extent to which FFLM succeeds in achieving its targets remains to be seen.
- FFLM maintains good asset quality with limited fresh infection in recent years. The chronic non-performing loan book is fully provided, and the management does not foresee any further recoveries. Although FFLM has high concentration in its finances, the related risk is managed through strong security structure and effective monitoring.
- Given the Modaraba's earlier cautious approach towards growth and existing scale of operations, it did not maintain a large funding base. FFLM usually gets funding under *musharaka* and *morabaha* arrangements. However, the Modaraba's funding base is normally concentrated with one or two institutions.
- FFLM's investments comprise: (i) equity portfolio (ii) properties. There has been a loss of ~ PKR 20mln on its investments in stocks, of which PKR 5mln has been provided in P&L at end-Mar09 and PKR 15mln routed through equity as per regulatory provisions. Meanwhile, properties, a combination of land and building, carry a significant unrecognized revaluation surplus.
- FFLM has a low leveraged capital structure which was augmented by a higher amount of retention (30%) during FY08. The Modaraba has shelved its plan for the issuance of *sukuk* (PKR 200mln) until recovery in the economy and stabilization of interest rates and liquidity in the market.

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. While the Modaraba operates principally through its head office in Lahore, it also has a branch in Islamabad. The Chief Executive of the Modaraba and his associates hold the majority shareholding in the management company of the Modaraba.
- The board of directors, chaired by Mr. Siyyid Tahir Nawazish, comprises five members including the Chief Executive Officer. The CEO, Mr. Wasim-ul-Haq Osmani, a Chartered Accountant with extensive experience in the financial sector, has been with the Modaraba since 1994.