

RATING REPORT

SME Leasing Limited (SLL)

REPORT DATE:

July 14, 2015

RATING ANALYSTS:

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RATING DETAILS

Rating Category	Latest Rating		Previous Rating	
	Long-term	Short-term	Long-term	Short-term
Entity	BB-	B	BB+	B
Rating Outlook	Negative		Stable	
Rating Date	Jul 09, '15		Aug 15, '14	

COMPANY INFORMATION

Incorporated in 2002	External Auditors: M/s KPMG Taseer Hadi & Company– Chartered Accountants
Public Listed Company	Chairman of the Board: Ms. Mehnaz Kaludi
Key Shareholders (with stake 5% or more):	Chief Executive Officer: Mr. Mir Javed Hashmat
SME Bank Limited – 73.1%	

APPLICABLE METHODOLOGY(IES)

JCR-VIS Entity Rating Criteria: Non-Bank Financial Companies <http://jcrvis.com.pk/Images/NBFC.pdf>
 Linkages between Parent and Subsidiary companies http://jcrvis.com.pk/Images/criteria_parent.pdf

SME Leasing Limited (SLL)

OVERVIEW OF
THE INSTITUTION

SLL is a subsidiary of SME Bank Limited, which has a stake of 73.1% in the company. SLL is listed on the Lahore stock Exchange. The company is operating with a network of 5 branches.

RATING RATIONALE

On-going losses for the past several years have resulted in the erosion of the equity base of SME Leasing Limited (SLL); in the absence of fresh injection of equity, the risk profile of the company stands diminished. SLL's equity is also short of the minimum capital requirement (MCR) of Rs. 700m stipulated for Non-Banking Finance Companies (NBFCs) undertaking business of leasing; the shortfall was reported at Rs. 512.5m at end-1QFY15. In view of the challenges faced by the NBFCs sector, a reform committee had proposed various revisions in the regulatory framework for NBFCs including lower MCR; further developments in lieu of the regulatory regime are awaited.

SLL is a majority owned subsidiary of SME Bank Limited (SMEBL). In the absence of other sources of funding, SMEBL remains the primary creditor of SLL. Management is in talks with SMEBL to convert a portion of the outstanding amount under the running finance facility into equity. As per the revised prudential regulations of SBP, maximum exposure limit of a bank to its related party has been capped at 7.5% of bank's equity (current outstanding constitutes around 30% of equity). This may severely restrict SLL's access to funding; SMEBL is seeking relaxation from the regulator in this regard. Moreover, risk profile of SMEBL has also diminished owing to continuous erosion of equity base.

Liquidity profile of SLL has come under significant stress over time on account of weak portfolio quality and lack of access to market sources of funding. Moreover, the company remained restricted from raising deposits from the general public by the Securities & Exchange Commission of Pakistan (SECP).

Lease disbursement significantly picked up pace, primarily in the first-half of the out-going year and contributed to the increase in the asset base. Disbursement activities slowed down in 1Q15 given that majority of funds were diverted towards meeting contractual payments against the running finance facility. Asset quality indicators remained stressed with majority of the portfolio being classified. Net infection stands lower due to increase in portfolio volume and was reported at 43.3%. Given the erosion in equity base, net NPL's as a proportion of Tier 1 Equity of 71.2% are sizeable, as of 1Q15 (FY14: 68.9%, FY13: 67.6%) reflecting a weak risk absorption capacity; in the absence of injection of fresh equity the same is expected to rise. Moreover, sizeable portion of the portfolio includes fresh disbursements made in FY14; asset quality would be more evident as the portfolio seasons.

Bottom-line was reported at a loss of Rs. 11.1m in the out-going year (FY13: Loss Rs. 7.4m). Despite significantly higher income from operations on the back of volumetric growth in earning assets, a larger cost base and higher provisioning charges vis-à-vis preceding year translated into a negative bottom-line. Management, while projecting subdued lending activity in FY15 with focus primarily on recoveries, is also working towards revision of policies and strengthening of risk management.

SME Leasing Limited (SLL)

Appendix I

FINANCIAL SUMMARY		(amounts in PKR millions)		
<u>BALANCE SHEET*</u>	DEC 31, 2014	DEC 31, 2013	DEC 31, 2012	
Total Investments	3.2	3.9	3.8	
Net Investment in Leases	247.0	186.3	208.2	
Total Assets	386.2	268.5	313.6	
Borrowings	159.8	43.9	80.8	
COI	-	0.2	8.3	
Subordinated Loans	-	-	-	
Tier-1 Equity	188.5	199.5	207.8	
Net Worth	190.5	200.3	207.9	
<i>*Where applicable, figures are net of lease key money</i>				
<u>INCOME STATEMENT</u>	DEC 31, 2014	DEC 31, 2013	DEC 31, 2012	
Net Mark-up Income	46.1	26.2	44.9	
Net (Provisioning) / Reversal	(2.3)	0.9	13.4	
Operating Expenses	37.9	29.4	40.6	
Profit (Loss) Before Tax	(10.6)	(7.4)	(28.9)	
Profit (Loss) After Tax	(11.1)	(7.7)	(29.1)	
<u>RATIO ANALYSIS</u>	DEC 31, 2014	DEC 31, 2013	DEC 31, 2012	
Gross Infection (%)	56.6	74.3	73.9	
Provisioning Coverage (%)	55.9	54.6	50.3	
Net Infection (%)	43.3	56.4	58.1	
Efficiency (%)	82.4	112.3	90.6	
ROAA (%)	-3.4	-2.7	-7.8	
ROAE (%)	-5.6	-3.8	-13.1	
Current Ratio (x)	1.1	1.5	1.5	

ISSUE/ISSUER RATING SCALE & DEFINITIONS

Appendix II

Medium to Long-Term**AAA**

Highest credit quality; the risk factors are negligible, being only slightly more than for risk-free Government of Pakistan's debt.

AA+, AA, AA-

High credit quality; Protection factors are strong. Risk is modest but may vary slightly from time to time because of economic conditions.

A+, A, A-

Good credit quality; Protection factors are adequate. Risk factors may vary with possible changes in the economy.

BBB+, BBB, BBB-

Adequate credit quality; Protection factors are reasonable and sufficient. Risk factors are considered variable if changes occur in the economy.

BB+, BB, BB-

Obligations deemed likely to be met. Protection factors are capable of weakening if changes occur in the economy. Overall quality may move up or down frequently within this category.

B+, B, B-

Obligations deemed less likely to be met. Protection factors are capable of fluctuating widely if changes occur in the economy. Overall quality may move up or down frequently within this category or into higher or lower rating grade.

CCC

Considerable uncertainty exists towards meeting the obligations. Protection factors are scarce and risk may be substantial.

CC

A high default risk

C

A very high default risk

D

Defaulted obligations

Short-Term**A-1+**

Highest certainty of timely payment; Short-term liquidity, including internal operating factors and /or access to alternative sources of funds, is outstanding and safety is just below risk free Government of Pakistan's short-term obligations.

A-1

High certainty of timely payment; Liquidity factors are excellent and supported by good fundamental protection factors. Risk factors are minor.

A-2

Good certainty of timely payment. Liquidity factors and company fundamentals are sound. Access to capital markets is good. Risk factors are small.

A-3

Satisfactory liquidity and other protection factors qualify entities / issues as to investment grade. Risk factors are larger and subject to more variation. Nevertheless, timely payment is expected.

B

Speculative investment characteristics; Liquidity may not be sufficient to ensure timely payment of obligations.

C

Capacity for timely payment of obligations is doubtful.

Rating Watch: JCR-VIS places entities and issues on 'Rating Watch' when it deems that there are conditions present that necessitate re-evaluation of the assigned rating(s). Refer to our 'Criteria for Rating Watch' for details. www.jcrvis.com.pk/images/criteria_watch.pdf

Rating Outlooks: The three outlooks 'Positive', 'Stable' and 'Negative' qualify the potential direction of the assigned rating(s). An outlook is not necessarily a precursor of a rating change. Refer to our 'Criteria for Rating Outlook' for details. www.jcrvis.com.pk/images/criteria_outlook.pdf

(SO) Rating: A suffix (SO) is added to the ratings of 'structured' securities where the servicing of debt and related obligations is backed by some sort of financial assets and/or credit support from a third party to the transaction. The suffix (SO), abbreviated for 'structured obligation', denotes that the rating has been achieved on grounds of the structure backing the transaction that enhanced the credit quality of the securities

and not on the basis of the credit quality of the issuing entity alone.

'p' Rating: A 'p' rating is assigned to entities, where the management has not requested a rating, however, agrees to provide informational support. A 'p' rating is shown with a 'p' subscript and is publicly disclosed. It is not modified by a plus (+) or a minus (-) sign which indicates relative standing within a rating category. Outlook is not assigned to these ratings. Refer to our 'Policy for Private Ratings' for details. www.jcrvis.com.pk/images/policy_ratings.pdf

'SD' Rating: An 'SD' rating is assigned when JCR-VIS believes that the ratee has selectively defaulted on a specific issue or obligation but it will continue to meet its payment obligations on other issues or obligations in a timely manner.

REGULATORY DISCLOSURES				Appendix III	
Name of Rated Entity	SME Leasing Limited (SLL)				
Sector	Non-Bank Financial Institution (NBFC)				
Type of Relationship	Solicited				
Purpose of Rating	Entity Rating				
Rating History	Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
	RATING TYPE: ENTITY				
	09-Jul-15	BB-	B	Negative	Downgrade
	15-Aug-14	BB+	B	Stable	Reaffirmed
	03-Jul-13	BB+	B	Stable	Downgrade
	05-Jul-12	BBB-	A-3	Negative	Downgrade
	02-Aug-11	BBB	A-3	Negative	Downgrade
Instrument Structure	N/A				
Statement by the Rating Team	JCR-VIS, the analysts involved in the rating process and members of its rating committee do not have any conflict of interest relating to the credit rating(s) mentioned herein. This rating is an opinion on credit quality only and is not a recommendation to buy or sell any securities.				
Probability of Default	JCR-VIS’ ratings opinions express ordinal ranking of risk, from strongest to weakest, within a universe of credit risk. Ratings are not intended as guarantees of credit quality or as exact measures of the probability that a particular issuer or particular debt issue will default.				
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