RATING REPORT

SME Leasing Limited (SLL)

REPORT DATE:
July 01, 2016

RATING ANALYSTS:
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RATING DETAILS

	Latest Rating		Previous Rating	
Rating Category	**Long-term**	**Short-term**	**Long-term**	**Short-term**
Entity	B	B	BB-	B
Rating Outlook	Negative		Negative	
Rating Date	*Jul 01, '16*		*Jul 09, '15*	

COMPANY INFORMATION

Incorporated in 2002	**External Auditors:** M/s Grant Thornton Anjum Asim Shahid Rahman, Chartered Accountants
Public Listed Company	**Chairman of the Board**: Ms. Mehnaz Saleem
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	RATING RATIONALE

In 2002, SME Leasing Limited (SLL) was incorporated as an unlisted public company. SLL is a subsidiary of SME Bank Limited (SMEBL), the main sponsor, which holds 73.1% of the company's shares. External auditors of the company for CY15 were M/s KPMG Taseer Hadi & Company, Chartered Accountants.

SME Leasing Limited (SLL) is a majority owned subsidiary of SME Bank Limited (SMEBL). SLL is engaged in provision of lease and working capital financing to small and medium sized businesses. The company operates through a network of 6 branches across the country including its head office in Karachi.

Rating Drivers:

- **Sponsor Profile:** SLL's parent, SMEBL is majority owned by the Government of Pakistan. Assigned ratings incorporate weakening in risk profile of SMEBL due to continuous erosion of equity base which has led to substantial downgrade of the parent's credit rating in 2016. As a result, SMEBL's ability to provide funding in the form of running finance (RF) facility to SLL stands diminished.

- **Funding:** In order to fund its operations, SLL solely utilizes RF facility provided by SMEBL. This RF facility is non-compliant from SMEBL's perspective on which a relaxation is available up to June 30, 2016. In view of this, RF facility currently remains available to the leasing company. Management expects that SMEBL would be exempted from this condition till June 30, 2017. Nevertheless, funding constraints restrict the ability of SLL to book fresh business.

- **Disbursements:** Given the subpar quality of financing disbursed in CY14, management resorted to consolidation of existing portfolio. Lending activity was therefore subdued in CY15. Recoveries have improved in the last two years. Going forward, disbursement is expected to continue with focus on recoveries.

- **Liquidity:** Liquid assets in relation to total liabilities are on the lower side. Asset quality indicators remained stressed with majority of portfolio being classified. In the absence of fresh equity, net NPLs as a proportion of Tier 1 Equity are sizeable. Risk management framework and controls in place for recovery have been improved in the outgoing year.

- **Capitalization:** Net equity has continued its downward trend on account of year-on-year losses being reported by the company. As per the revised NBFC Regulations 2008, minimum equity requirement for non-deposit taking leasing companies has been set at Rs. 50.0m. SLL has opted to operate without accepting deposits; therefore, it is in compliance with regulatory capital requirements. Nevertheless, capitalization indicators remain weak and limit the institution's risk absorption capacity.

- **Profitability:** Bottom-line was reported at a loss of Rs. 17.3m in CY15 (CY14: Loss of Rs. 11.1m). Continued trend in losses was observed on account of drop in income from operations coupled with sizeable fixed costs. By end-1Q16, SLL posted earnings of Rs. 0.6m on the back of recoveries against NPLs.

Outlook

Risk profile of the company is contingent upon availability of financing from the parent. In case of withdrawal of RF line, losses may continue to accumulate in view of subdued lending activity and piling up of NPLs; recovery efforts on part of management may enable the company to generate cash flow to fund its operations.

SME Leasing Limited (SLL) — Appendix I

FINANCIAL SUMMARY *(amounts in PKR millions)*			
BALANCE SHEET*	**1Q16**	**31-Dec-15**	**31-Dec-14**
Total Investments	3.5	4.3	3.2
Net Investment in Leases	470.0	458.7	520.1
Total Assets	334.1	327.2	386.2
Borrowings	137.2	129.4	156.6
COI	-	-	-
Subordinated Loans	-	-	-
Tier-1 Equity	171.9	171.3	188.5
Net Worth	174.2	174.4	190.5
****Where applicable, figures are net of lease key money***			
INCOME STATEMENT	**1Q16**	**31-Dec-15**	**31-Dec-14**
Net Mark-up Income	13.1	27.7	46.1
Net (Provisioning) / Reversal	-0.03	5.9	-2.3
Operating Expenses	8.9	37.3	37.9
Profit (Loss) Before Tax	0.7	-21.1	-10.6
Profit (Loss) After Tax	0.6	-17.3	-11.0
RATIO ANALYSIS	**1Q16**	**31-Dec-15**	**31-Dec-14**
Gross Infection (%)	75.8	78.1	56.6
Provisioning Coverage (%)	44.5	44.2	55.8
Net Infection (%)	63.4	66.5	36.5
Efficiency (%)	85.4	134.4	82.4
Gearing (%)	0.79	0.74	0.82
Debt Leverage (%)	0.92	0.88	0.65
ROAA (%)	0.2	-4.8	-3.4
ROAE (%)	0.3	-9.5	-5.6

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	see table below
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.
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Rating History

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
RATING TYPE: ENTITY				
01-Jul-16	B	B	Negative	Downgrade
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