



The Pakistan Credit Rating Agency Limited

ORIX MODARABA RATING REPORT

	NEW [JUL-17]	INITIAL [JAN-17]
Long-Term	AA	AA
Short-Term	A1+	A1+
Outlook	Stable	Stable

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JULY 2017

Profile & Ownership

- An Islamic financial institution, established in 1987
- Primarily engaged in financing of plant, machinery and vehicles through ijarah and musharika, and housing via musharaka
- Standard chartered bank (Pakistan) Limited, as part of its divestment strategy sold its 100% shares of Standard Chartered Services of Pakistan (Pvt.) limited and its 20% (direct & indirect) stake in ORIX Modaraba to ORIX Leasing Pakistan (OLP).
- Modaraba Management Company and Modaraba operate as in ORIX Services Pakistan (Pvt.) Limited (OSPL) and ORIX Modaraba respectively.
- ORIX Leasing Pakistan Limited holds 20% ownership stake in ORIXM through OSPL.
- Listed on Pakistan Stock Exchange

Governance & Management

- BoD comprises six members including the CEO.
- Four board members are ex-officio nominees of OLP.
- Chairman Shaheen Amin, CEO of OLP, has extensive experience of over 30 years. Board has made two committees namely Audit committee and Human Resource & Remuneration committee both chaired by an independent director.
- Mr. Raheel Qamar Ahmad is CEO since 2011 and has over 25 years of experience in corporate and investment banking.
- Lean organizational structure with a professional management team.

Risk Management

- Comprehensive risk management systems in place.
- Financing book majorly comprises Ijarah (9MFY17: 80%; FY16: 77%; FY15: 77%).
- Ijarah portfolio dominated by corporate segment (90%) while diminishing musharika mainly comprises individuals (60%) during FY16.
- High top 20 credit concentration in financing book (ijarah: 50%; diminishing musharika: 62%) during FY16.
- NPLs as percentage of finances (9MFY17: 1.8%; FY16: 2.0%; FY14: 5.0%) have improved over period owing to recovery of PKR 11mln.

Performance

- During 9MFY17, ORIXM's spread declined 5.6% (FY16: 7.1; FY15: 8.3%; FY14:8.4%) owing to decline in asset yield 7.6% (FY16: 9.1%; FY15: 11%; FY14: 11.3%).
- Decreased ijarah rental is the main reason of decrease in revenue however reversal of provisions and other income helped the Modaraba to register strong though decreased net income (9MFY17: PKR 99mln; FY16: PKR 173mln; FY15: 195mln).
- Going forward, the management intends to enhance its overall portfolio taking comfort from new sponsor's expansion strategy. In this regard SMEs would remain key focus in the near future. Moreover, management also plans to increase its share in diminishing Musharika to 40%.

Financial Risk

- ORIXM's funding mix consists of one main source: Certificates of Musharika (92%) and other is Musharika financing (8%) during 9MFY17.
- Diversified funding base as CoMs are mainly mobilized from individuals (78%) followed by corporates (22%).
- Limited exposure to interest rate risk given the financing book and COMs are linked with floating rates.
- Higher concentration risk as top ten CoMs increased significantly to 53% in 9MFY17 (FY16: 38%; FY15: 14%).
- Maintained high leveraged capital structure (Debt to Equity ratio: 9MFY7: 2.9x; FY16: 2.7x; FY15: 2.7x).

RATING RATIONALE

ORIX Modaraba enjoys sound financial profile emanating from low leveraging, managed liquidity, and sustained profitability. Moreover, good management quality, strong risk management systems and control environment provide strength to ORIXM's profile. The Modaraba maintains its healthy performance - particularly asset quality and profitability. The management's new business strategy envisages volumetric growth in assets to improve its performance trends. The expected growth would be funded through mix of internal sources and debt. However, the management expects to maintain the leveraging pattern at comfortable level. The Modaraba's affiliation with ORIX Leasing Pakistan Limited helps in further strengthening the risk management, providing established outreach and experience of parent, particularly in SME segment, which the management of Modaraba has identified as key growth driver.

KEY RATING DRIVERS

The ratings are dependent on the management's ability to sustain its strong financial profile while ensuring stable profitability.

INDUSTRY SNAPSHOT

- 25 Modarabas
- Intense competition from established financial institutions (FIs) owing to small network and similar nature of products being offered by these FIs.
- High threat of new entrants owing to small capital investment
- SECP grants authorization to float two new Modaraba of PKR 800mln.



The Pakistan Credit Rating Agency Limited

Orix Modaraba	<i>PKR mln</i>			
BALANCE SHEET	31-Mar-17	30-Jun-16	30-Jun-15	30-Jun-14
	9M	Annual	Annual	Annual
Assets				
Finances				
a) Musharika Financing	1,011	1,199	1,063	1,206
b) Investment in Ijarah Finance	4,167	3,638	3,539	4,195
c) Sukuks	-	-	-	-
Deposits with banks	217	217	248	124
Other Non Earning Assets	233	223	227	364
Non-Performing Finances	94	98	240	274
Less: Provision for Doubtful Receivables	(94)	(98)	(137)	(127)
Net Non-Performing Finances	-	-	103	147
Total Assets	5,626	5,278	5,180	6,035
Liabilities				
Funding				
a) Certificates of Mushariks	3,026	2,794	2,684	2,774
b) Morabaha Financing	-	-	-	-
c) Musharika Financing	249	328	478	1,041
d) Lease Rentals received in Advance	812	712	623	838
Other Liabilities	419	267	243	288
Equity				
Total Equity	1,120	1,176	1,153	1,094
TOTAL LIABILITIES & EQUITY	5,626	5,278	5,180	6,035
INCOME STATEMENT				
Gross Revenue	303	468	587	655
Financial Charges	(156)	(223)	(313)	(386)
Other Income	40	27	66	35
Operating Expense	(89)	(113)	(103)	(95)
Pre-provision Profit	98	160	236	209
Provision for doubtful Receivables	11	33	(18)	(6)
Management Fee	(10)	(20)	(23)	(21)
Net Income	99	173	195	182
Ratio Analysis				
Profitability Ratios				
ROA	2.4% *	3.3%	3.5%	2.8%
Cost-to-Total Net Revenue	47.7%	41.4%	30.4%	31.2%
Capital Adequacy				
Equity / Total Assets	19.9%	22.3%	22.3%	18.1%
Funding & Liquidity				
Short Term Funding/Total Funding	87.8%	73.3%	84.4%	84.4%
Loan Loss Coverage				
Impaired Lending/Gross Finances	1.8%	2.0%	5.0%	4.8%
Net Impaired Lending/Total Equity	8.4%	8.4%	20.8%	25.1%

*Annualized

Orix Modaraba

Jul-17

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CREDIT RATING SCALE & DEFINITIONS

Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

LONG TERM RATINGS		SHORT TERM RATINGS
AAA	Highest credit quality. Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments.	A1+: The highest capacity for timely repayment. A1: A strong capacity for timely repayment. A2: A satisfactory capacity for timely repayment. This may be susceptible to adverse changes in business, economic, or financial conditions. A3: An adequate capacity for timely repayment. Such capacity is susceptible to adverse changes in business, economic, or financial conditions. B: The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions. C: An inadequate capacity to ensure timely repayment.
AA+	Very high credit quality. Very low expectation of credit risk.	
AA	Indicate very strong capacity for timely payment of financial commitments. This capacity is not significantly vulnerable to foreseeable events.	
AA-		
A+	High credit quality. Low expectation of credit risk.	
A	The capacity for timely payment of financial commitments is considered strong. This capacity may, nevertheless, be vulnerable to changes in circumstances or in economic conditions.	
A-		
BBB+	Good credit quality. Currently a low expectation of credit risk.	
BBB	The capacity for timely payment of financial commitments is considered adequate, but adverse changes in circumstances and in economic conditions are more likely to impair this capacity.	
BBB-		
BB+	Moderate risk. Possibility of credit risk developing.	
BB	There is a possibility of credit risk developing, particularly as a result of adverse economic or business changes over time; however, business or financial alternatives may be available to allow financial commitments to be met.	
BB-		
B+	High credit risk.	
B	A limited margin of safety remains against credit risk. Financial commitments are currently being met; however, capacity for continued payment is contingent upon a sustained, favorable business and economic environment.	
B-		
CCC	Very high credit risk. Substantial credit risk	
CC	“CCC” Default is a real possibility. Capacity for meeting financial commitments is solely reliant upon sustained, favorable business or economic developments. “CC” Rating indicates that default of some kind appears probable. “C” Ratings signal imminent default.	
C		
D	Obligations are currently in default.	

Outlook (Stable, Positive, Negative, Developing)
Indicates the potential and direction of a rating over the intermediate term in response to trends in economic and/or fundamental business/financial conditions. It is not necessarily a precursor to a rating change. ‘Stable’ outlook means a rating is not likely to change. ‘Positive’ means it may be raised. ‘Negative’ means it may be lowered. Where the trends have conflicting elements, the outlook may be described as ‘Developing’.

Rating Watch
Alerts to the possibility of a rating change subsequent to, or in anticipation of, a) some material identifiable event and/or b) deviation from expected trend. But it does not mean that a rating change is inevitable. A watch should be resolved within foreseeable future, but may continue if underlying circumstances are not settled. Rating Watch may accompany Outlook of the respective opinion.

Suspension
It is not possible to update an opinion due to lack of requisite information. Opinion should be resumed in foreseeable future. However, if this does not happen within six (6) months, the rating should be considered withdrawn.

Withdrawn
A rating is withdrawn on a) termination of rating mandate, b) cessation of underlying entity, c) the debt instrument is redeemed, d) the rating remains suspended for six months, e) the entity/issuer defaults, or/and f) PACRA finds it impractical to surveil the opinion due to lack of requisite information

Disclaimer: PACRA's ratings are an assessment of the credit standing of entities/issue in Pakistan. They do not take into account the potential transfer / convertibility risk that may exist for foreign currency creditors. PACRA's opinion is not a recommendation to purchase, sell or hold a security, in as much as it does not comment on the security's market price or suitability for a particular investor.



Name of Rated Entity
Sector
Type of Relationship

Orix Modaraba
Modaraba
Solicited

Purpose of the Rating

Independent Risk Assessment

Rating History

Dissemination Date	Long Term	Short Term	Outlook	Action
31-Jul-17	AA	A1+	Stable	Maintain
14-Jan-17	AA	A1+	Stable	Initial

Related Criteria and Research
Sector Research

NBFC's and Modaraba Sector - Viewpoint | Mar17

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Rating Procedure

Rating is an opinion on relative credit worthiness of an entity or debt instrument. It does not constitute recommendation to buy, hold or sell any security. The rating team for this assignment does not have any beneficial interest, direct or indirect in the rated entity/instrument.

[Disclaimer](#)

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[Probability of Default \(PD\)](#)

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