

## First Punjab Modaraba (FPM)

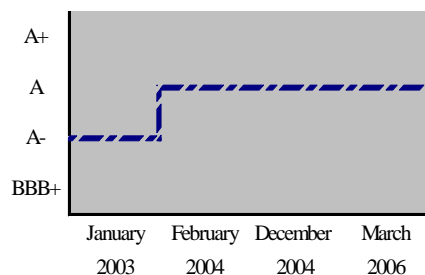
### Ratings (April 2006)

First Punjab Modaraba

Entity	New	Previous
Long Term	A	A
Short Term	A1	A1
<b>Outlook</b>	<b>Positive</b>	

### L.T. Entity Rating History

#### Financial Data



PKR (mln)

	31-Dec-05 1HFY06)*	30-Jun-05	30-Jun-04
Total Assets	1,622.9	1,325.2	1,039.8
Equity	465.0	427.6	418.0
Profit after Tax	37.3	53.9	64.2
ROA %	5.06	4.56	7.83
ROE %	16.73	12.75	15.56
Equity/Assets %	28.65	32.27	40.20

\* 1HY2006 figures are based on un-audited accounts, and relevant ratios have been annualised for meaningful comparison.

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### Rating Rationale

#### Assessment

FPM's ratings reflect its sustained good asset quality and strong capacity to absorb potential risk. The ratings also recognize the improving trend in performance witnessed post FY05 with increasing contribution of non-mark up based earnings. The management's ongoing strategy of leveraged volume expansion, facilitated by access to required funding is likely to improve earning prospects. These would also be augmented by income from non-core operations. The future outlook, therefore, appears to be positive. Meanwhile, affiliation with BoP continues to be a key rating factor.

In FY05, FPM maintained growth in its finance portfolio, though the growth rate was lower compared to last year. However, the benefit of volume growth could not be fully translated into net revenues due to substantial decline in spreads. The Modaraba could not increase its asset yield in line with soaring financial cost amidst increasing interest rate environment. Moreover, it could not replicate the high level of capital gains, resulting in the YoY decline in the bottom line. The Modaraba maintained its growth momentum in the first half of FY06, and gross finances increased by 32% in line with the target for FY06. However, spreads remained under constant pressure owing to the continuous hike in borrowing cost, which had a negative bearing on Modaraba's net interest revenues. The impact was more than offset by other operating income due largely to hefty capital gains and advisory fee.

Going forward, in order to compensate for falling interest margins, the management plans to continue taking leveraged volume expansion while strengthening its niche market through providing facilities to untapped and non-traditional SME and consumer clusters. Though it is inherently more risk prone, efforts are underway to strengthen the overall risk management systems. The new credit policy, under implementation, will be more transparent introducing the delegation of authority to specified levels in the hierarchy. The targeted growth is planned to be facilitated through increasing geographical outreach. To achieve the future targets, a sustainable human resource is required, which has been an impediment for the Modaraba recently. The management is conscious of the need to strengthen the area even if that entails increase in the personnel cost. Meanwhile, the income stream from investment portfolio and financial advisory services is likely to continue contributing towards the bottom line.

The asset quality of FPM continues to be outstanding, with full provisioning against NPLs, and with no fresh infection since FY04. While there is little likelihood of erosion in profitability on this account, the management is proactively pursuing recovery and settlement against chronic classified cases. However, credit concentration remains a concern, with the top ten exposures comprising more than 70% of total financing portfolio. Similarly, the sector concentration is also high, though declining from last year, as the textile sector constitutes around 34% of the total finance portfolio. Given the higher focus on the SME sector, both client and sectoral concentrations are likely to decrease. Meanwhile, the strong risk absorption capacity and effective risk management as demonstrated so far provide reasonable comfort against potential risk.

Musharika based credit lines from BoP have historically been the major source of FPM's funding, representing more than half of the total funding of the Modaraba. During FY05, the Modaraba started diversifying its funding base through issuing Certificates of Musharika (COMs). The increasing gearing level is in line with the growing asset base. However, in order to strengthen the capital structure, the management is planning to issue right certificates in the future.

#### Support

While BoP has no contractual obligation to support FPM, owing to close institutional linkage and the use of the bank's name, in PACRA's view, support would be forthcoming should it prove necessary.

#### Background

Established in 1992, FPM is a perpetual, multi-purpose Modaraba, listed on all three bourses in the country. It is primarily engaged in morabaha and lease financing and operates from a single location in Lahore.

The Modaraba is managed by Punjab Modaraba Services (Pvt.) Ltd holding around 38% stake in the Modaraba. The management company of the Modaraba is a wholly owned subsidiary of The Bank of Punjab (BoP), which is a large commercial bank in which the Government of Punjab holds majority stake. The board of the management company comprises five directors; all are nominees of the BoP. The Chief Executive of the Modaraba, appointed in FY05, possesses around 10 years of experience in the banking sector and enjoys complete operational autonomy.