

## RATING REPORT

### Trust Modaraba

**REPORT DATE:**

April 26, 2022

**RATING ANALYSTS:**

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Muhammad Taha

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	Latest Rating	Previous Rating
<b>Rating Category</b>		
<b>Entity</b>	BBB+ / A-2	BBB- / A-3
<b>Rating Date</b>	April 26, '22	Feb 17, '21
<b>Rating Outlook</b>	Stable	Stable

**COMPANY INFORMATION**

<b>Incorporated in 1991</b>	<b>External Auditors:</b> Grant Thornton Anjum Rehman & Co. Chartered Accountants
<b>Public Listed Company</b>	<b>Chairman:</b> Mr. Shaikh Arshad Farooq
	<b>Chief Executive Officer:</b> Mr. Basheer Ahmed Chowdry

**APPLICABLE METHODOLOGY(IES)**

VIS Entity Rating Criteria: Non-Bank Financial Companies (March, 2020)

<http://vis.com.pk/kc-meth.aspx>

## Trust Modaraba

## OVERVIEW OF THE INSTITUTION RATING RATIONALE

*Trust Modaraba (TM) was incorporated in 1991 under Mordaraba companies and Modaraba (flotation and control) Ordinance. TM is listed on Pakistan Stock Exchange with its head office located in Karachi. Financial Statements of the modaraba for FY21 were audited by Crowe Hussain Chaudhury & Co. Chartered Accountants.*

Since 2009, Trust Modaraba (TM) has been managed by Al-Zamin Modaraba Management (Private) Limited (AZMM). TM is currently engaged in Ijarah, Morabaha, Musharakah, and equity market operations. Majority certificate holding of the Modaraba is vested with an individual, Mr. Mohammad Aslam Motiwala (56.8%) followed by 17.7% interest by AZMM. In the longer run, the management is currently considering options pertaining to merger with other small Modaraba organizations, which will allow an increase in customer financing portfolio due to the availability of additional funds. However, no such concrete plan has been devised in this regard.

**Key Rating Drivers**

**Asset mix depicts higher exposure to financings.**

Rs. in millions	FY19	FY20	FY21	1HFY22
Financing (including Ijarah's FA)	290	254	270	311
Short term investments	8	18	26	35
Investment properties	14	20	22	9
Other assets	59	65	60	57
<b>Total Assets</b>	<b>371</b>	<b>358</b>	<b>379</b>	<b>411</b>

Overall asset base of the entity has increased to Rs. 411m (FY21: Rs. 379m, FY20: Rs. 358m) at end-1HFY22. Financing portfolio continues to dominate the asset mix with the company's stringent efforts to increase its Ijarah and Morabaha portfolio. Investment in properties has been reduced by disposing on account of management's strategic decision to deploy funds in core operations. Investment property portfolio comprises of exposure in land, agricultural land and shop in Faisalabad, Gujranwala and Hyderabad. Short-term investments portfolio has depicted an upward trend on a timeline basis; however, the plan going forward is to liquidate a proportion of the same at profitable values and maintain a minimum portfolio to the tune of Rs. 25m.

**Portfolio credit quality has shown improvement, due to the settlement of a Non-Performing Financing (NPF) and a shift from SMEs to corporates.**

After reporting a decline in FY21, gross financing portfolio witnessed growth in the ongoing year and was reported at Rs. 329m (FY21: Rs. 287m, FY20: Rs. 308m) at end-Dec'21. Growth in the portfolio was contributed by a 30% increase in Ijarah financing and 14% increase in Morabaha financing. These two modes of financing continue to comprise 90% of the overall gross financing portfolio. Furthermore, as a result of management's conscious strategy, a shift has been observed in the client profile with 69% of the financing book comprising of corporate clients followed by individuals contributing 23% and SMEs providing 8.5% to the portfolio.

Going forward, management envisages to maintain a mix of corporate and SME clients, managing their credit risk profile without significantly affecting its margins. Moreover, the company also plans to participate in housing development projects prudently.

During 1HFY22, management successfully finalized an out of court settlement of Rs. 50 million for a litigated account in Lahore. This has taken the total recoveries from the portfolio inherited by the existing management to Rs. 154m to date. Management expects further recoveries of about Rs. 25-30m this year and Rs. 50m in FY23 from two big customers (Prime Traders, Al-Rai Roller Flour Mills). Furthermore, shift in portfolio mix towards corporate clients has improved the credit risk profile. Consequently, gross infection of the portfolio at end-FY21 and Dec'21 is noticeably lower as compared to FY20 (figures shown in the table below). However, management took advantage of the higher income booked in the first half to enhance the provisioning coverage at end-Dec'21. Net infection ratio also exhibited improvement on a timeline basis.

	FY20	FY21	1HFY22
Gross Infection*	40.1%	23.6%	12.3%
Provisioning Coverage*	49%	29%	53%
Net Infection*	25.3%	18.0%	6.2%
<i>*Net of customer security deposits</i>			

**Recovery efforts have paved the way for improvement in net income on a timeline basis**

Rs. in millions	FY20	FY21	1HFY22
<b>Operating Revenue</b>	<b>34.8</b>	<b>44.3</b>	<b>61.9</b>
Income on financing	28.4	26.3	17.9
Income from Investments	0.9	8.4	0.5
Trading Income	0.1	-	-
Other Income	5.4	9.6	43.5
<b>Operating Expenses</b>	<b>(30.5)</b>	<b>(36.4)</b>	<b>(19.9)</b>
Efficiency	88%	82%	32%
Other (Net)	-1.7	0.1	-22.3
<b>Profit Before tax</b>	<b>2.7</b>	<b>8.0</b>	<b>18.5</b>
<b>Profit After tax</b>	<b>1.7</b>	<b>6.6</b>	<b>14.6</b>

The entity posted consistent growth in its total revenue base with a sizeable surge noted in 1HFY22 led by gain on (a) settlement of a long outstanding account and (b) sale of vehicles earlier deployed under fleet operation project. Income from financing portfolio showed a slight improvement in annualized terms. However, the out of court settlement of an NPF permitted the company to sell a property for around Rs. 50m against a claim of about Rs.13m., with the surplus offering an additional source of income. Due to the increase in earnings, the management opted for a more prudent approach and recorded an additional provision of Rs. 10m during 1HFY22. Furthermore, due to a depressed performance of the equity market, an unrealized loss of Rs. 10m on equity investments was also recorded in 1HFY22. Operating

expenses increased by Rs.4m in 1HFY22; major increase of which was noted in staff salaries due to hiring of additional staff, and annual increment and payment of one-time fee of Rs.2.3m to SECP for increase in authorized capital. Despite additional expenses recorded, the company reported a higher profit after tax to the tune of Rs. 15m in 1HFY22 (FY21: Rs. 7m, FY20: Rs. 2m). Recently, a change in Modaraba regulations has resulted in the withdrawal of income tax exemption (if 90% of profit was distributed to certificate holders), which now has to be paid at a rate of 17.5%.

Going forward, management plans to increase the number of sectors that it caters to by entering the segment of low cost housing with minimal risk. It will also offer a chance for diversification by increasing the company's customer base in Lahore. Regulatory approvals are yet to be taken in this regard. The company also plans to attain a deposit license in the future. In addition to that, the imposition of a Rs. 3m limit on car financing by SBP has opened up a new market opportunity for the entity, and now it intends to offer diminishing Musharakah to those people who require financing in excess of that limit. Given the aforementioned growth factors and expected recovery from litigated accounts, profitability is projected to improve on a sustainable basis.

#### **A debt free capital structure.**

With no outstanding borrowings on the balance sheet, TM's leverage indicators continue to remain on the lower side. Higher profit retention led to an improvement in equity base, which went up to Rs. 331m at end-1HFY22. Liquidity profile is also considered adequate, with the proportion of liquid assets to current liabilities standing at 1.2x as of Dec'21. The company does have access to credit lines, but due to the relatively high mark-up rates considering its small-size, the same has not been utilized.

**Trust Modaraba (TM)**
**Appendix I**

Financial Summary (amounts in PKR millions)				
	FY19	FY20	FY21	1HFY22
Investments in Equities	13.7	27.5	36.6	42.8
Investment Property	13.7	20.4	22.3	8.6
Financing Portfolio (net)	290.2	253.6	270.2	310.9
Total Assets	371.3	357.5	378.8	411.0
Certificate Capital	298.0	298.0	298.0	298.0
Net Equity	303.9	306.9	315.6	326.8
<b>Income Statement</b>				
Income from ijarah	12.5	8.7	9.7	8.8
Profit on murabaha finances	11.5	11.7	10.8	5.7
Profit on musharakah finances	5.5	8.0	5.8	3.4
Income from investments - net	0.2	0.9	8.4	0.5
Trading income	1.8	0.1	-	-
Other income	2.1	5.4	9.6	43.5
<b>Total Income</b>	<b>33.6</b>	<b>34.8</b>	<b>44.3</b>	<b>61.9</b>
Net Provisioning/Reversal	(2.6)	(1.1)	1.1	(19.9)
Operating Expenses	(29.7)	(30.5)	(36.4)	(19.9)
Profit (Loss) Before Tax	1.2	2.7	8.0	18.5
Profit (Loss) After Tax	1.0	1.7	6.6	14.6
<b>Ratio Analysis</b>				
Gross Infection*	33.60%	40.20%	23.6%	12.3%
Net Infection*	18.80%	25.50%	18.0%	6.2%
Provisioning Coverage*	54.00%	49.20%	28.9%	52.6%
Leverage	0.22	0.17	0.20	0.25
Efficiency	88.40%	87.60%	82.2%	32.2%
ROA**	0.30%	0.50%	1.7%	7.1%
ROE**	0.30%	0.60%	2.1%	8.9%
Current Ratio	7.8	8.5	7.43	5.00

\*Net of Customer Security Deposits

\*\* Annualized

## ISSUE/ISSUER RATING SCALE & DEFINITIONS II

## Appendix

### RATING SCALE & DEFINITIONS: ISSUES / ISSUERS

#### 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:** 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.vis.com.pk/images/criteria\\_watch.pdf](http://www.vis.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.vis.com.pk/images/criteria\\_outlook.pdf](http://www.vis.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.

**(blr) Rating:** A suffix (blr) is added to the ratings of a particular banking facility obtained by the borrower from a financial institution. The suffix (blr), abbreviated for 'bank loan rating' denotes that the rating is based on the credit quality of the entity and security structure of the facility.

**'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.vis.com.pk/images/policy\\_ratings.pdf](http://www.vis.com.pk/images/policy_ratings.pdf)

**'SD' Rating:** An 'SD' rating is assigned when 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	
<b>Name of Entity</b>	Trust Modaraba				
<b>Sector</b>	Modaraba				
<b>Type of Relationship</b>	Solicited				
<b>Purpose of Rating</b>	Entity Rating				
<b>Rating History</b>	<b>Rating Date</b>	<b>Medium to Long Term</b>	<b>Short Term</b>	<b>Rating Outlook</b>	<b>Rating Action</b>
	<b><u>RATING TYPE: ENTITY</u></b>				
	26-April-22	BBB+	A-2	Stable	Upgrade
	17-Feb-21	BBB-	A-3	Stable	Maintained
	27-Aug-19	BBB-	A-3	-	Rating Watch - Negative
	26-Jan-18	BBB-	A-3	Stable	Maintained
	6-Dec-16	BBB-	A-3	Positive	Initial
<b>Instrument Structure</b>	N/A				
<b>Statement by the Rating Team</b>	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.				
<b>Probability of Default</b>	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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<b>Due Diligence Meetings Conducted</b>	<b>Name</b>	<b>Designation</b>		<b>Date</b>	
	Mr. Basheer Ahmed Chowdry	Chief Executive Officer		March 08, 2022	
	Ms. Hamida Aqeel	Chief Operating Officer/Company Secretary		March 08, 2022	