RATING REPORT

Sindh Modaraba

REPORT DATE:
June 30th, 2022

RATING ANALYSTS:
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RATING DETAILS

Rating Category	Latest Rating Long-term	Latest Rating Short-term	Previous Rating Long-term	Previous Rating Short-term
Entity	A+	A-1	A+	A-1
Rating Outlook	Stable		Stable	
Rating Date	*June 27, '22*		*June 29, '21*	
Rating Action	*Reaffirmed*		*Reaffirmed*	

MODARABA INFORMATION

Incorporated in 2015	**External auditors:** Baker Tilly Mehmood Idress Qamar Chartered Accountants
Public Listed Modaraba	**Chairman:** Mr. Waseem Mehdi Syed
Key Certificate holders (with stake 5% or more): Sindh Modaraba Management Limited - 94.36%	**Acting Chief Executive Officer:** Mr. Kamal Ahmed

APPLICABLE METHODOLOGY(IES)

JVIS Entity Rating Criteria: Non-Banking Financial Companies (March 2020)
http://vis.com.pk/kc-meth.aspx

Sindh Modaraba (SM)

OVERVIEW OF THE INSTITUTION

Sindh Modaraba (SM) has been incorporated under the Modaraba Companies and Modaraba (Floatation and Control) Ordinance, 1980. The Modaraba started its operations in 2015 and is managed by Sindh Modaraba Management Limited (SMML).

Profile of Chairman

Mr. Mehdi is currently serving as the Chairman and Independent Director of SM. Mr. Mehdi has over 40 years of experience within Financial sector. He is also Independent Director and Chairman of the Board of Directors of Summit Bank. Mr. Mehdi holds Master Degree from Karachi University and Diploma in Banking (DAIBP from) Institute of Banking in Pakistan.

RATING RATIONALE

Sindh Modaraba (SM) is managed by Sindh Modaraba Management Limited (SMML), which in turn, is owned by of Government of Sindh (GoS). SM is engaged in providing Shariah complaint financing facilities to customers. The Modaraba is listed on Pakistan Stock Exchange and its registered office is in Karachi. And operates through a network of two branches, one located in Karachi and the other based in Lahore.

Management Changes

In the ongoing year, sad demise of Chief Executive Officer, Mr. Zulfiqar Ali, left the position vacant which is expected to be filled within due course of time upon completion of all formal procedures and regulatory requirements. At present, acting CEO Mr. Kamal Ahmed (Non-Executive Director) is heading the Modaraba's operations.

Key Rating Drivers:

Ratings continue to remain underpinned by Sound Sponsor Profile

The key rating consideration is the sponsor profile of the Modaraba, GoS, which owns approximately 94.4% of SM's certificates through SMML. The remaining shareholding is vested within local individuals (5.28%), while the Directors, CEO and their spouses own less than 1 percent. The sponsor has demonstrated both technical and financial support for SM in the past. VIS considers continued sponsor support a key factor for ratings.

Portfolio growth remained slow in 9M'FY22. Going forward, timely appointment of CEO remains key.

Financing portfolio was reported lower at Rs. 677.1m (FY21: Rs. 819.6m; FY20: Rs. 791.9m) at the end of 9MFY22. As per management, the slowdown in financing activity was on account of change in management post CEO's demise. Timely appointment of new CEO remains key. As per SM's management, appointment of new CEO is in the final stages and will be completed in due course of time after compliance with all formal and regulatory requirement

Financing portfolio comprises primarily Diminishing Musharaka facility. Sector wise portfolio comprises increased exposure to Construction (FY21: 23.5%; FY20: 11.6%) and Transport (FY21: 7.8% FY20: 2.4%), while exposures in Sugar (FY21: 18.21%; FY20: 23.8%) and Food & Beverages (FY21: 12.82%; FY20: 16.6%) were reduced, although they still form major part of the portfolio. Fresh disbursements were recorded at Rs. 219.7m in FY21 and Rs. 82.2m during 9M'FY22. In order to rationalize and balance sector concentration, financing in FY22 has been targeted in the Health Care, Textile and Chemical sectors.

Asset quality indicators depict weakening

Non performing portfolio depicts increasing trend on timeline (9M'FY22: Rs. 46.0m; FY21: Rs. 44.9; FY20: Rs. 27.6m) resulting in significant jump in gross infection over the past years (9M'FY22: 6.8%; FY21: 5.5% FY20: 4.0%; FY20: 0.5%). Part of this was on account of introduction of stringent classification requirements for Modaraba companies in line with commercial banks and accumulated overdue rents of two major court cases customers of the Modaraba. Fresh NPLs were witnessed in retail and sugar sectors, albeit some recovery was also received in these accounts. Credit risk of the financing portfolio remains heightened due to external and internal vulnerabilities impacting business profits. Moreover, we expect additional provisioning pressure from the existing NPL portfolio which shall continue to constrain future profitability. Maintenance of asset quality indicators will remain key from ratings perspective.

Higher profits on liquid funds, not yet deployed, will provide support to pretax profitability, although tax charge on Modaraba companies may offset some of that benefit in the bottom line.

Profitability for the year FY21 decreased to Rs. 75.8m (FY20: Rs. 107.9m) on account of higher provisioning expense, reduced income from Musharaka financing and lower income generated from Bank deposits in the low interest rate period. However, in the ongoing year, with increase in interest rates, total income for 9MFY22 stood slightly higher at Rs. 115.6m (9MFY21: Rs. 105.4m) due to increase in weighted average return from 11.6% to 12.25%. Operating expenses were also lower during the ongoing fiscal year due to rationalizing of expenses. The pretax profitability in 9MFY22 has remained in line with full year FY21. Net profit, however, registered a declined with the introduction of tax charge effective FY22 onwards for Modaraba companies and was reported at Rs. 53.4.m (9MFY21: Rs. 97.2m) for 9MFY22. Going forward, uptick in yields is expected on both the financing portfolio as well as on deposit placements, supporting the overall profitability profile of SM.

Sound liquidity profile and capitalization indicators

Capitalization indicators of SM are considered sound as the Modaraba has not acquired any profit payment debt.

Liquidity profile of the Modaraba is sound given the sizable proportion of liquid assets at Rs. 971m mainly comprising cash in hand and short term investments. Short Term Investments worth Rs. 320m are invested in TDR in Sindh bank. Going forward, SM is looking to place surplus funds in TDR in other Islamic banks offering comparatively higher returns, which will support future profitability.

Sindh Modaraba (SM) Appendix I

FINANCIAL SUMMARY	*(amounts in PKR millions)*				
BALANCE SHEET	**FY18**	**FY19**	**FY20**	**FY21**	**9M'22**
Ijarah Assets	61.3	10.5	7.2	5.0	5.0
Current portion-Diminishing Musharaka	208.4	249.1	270.8	367.3	354.3
Long term portion-Diminishing Musharaka	407.0	407.1	514.0	447.3	317.8
Total Financing portfolio	676.7	666.7	791.9	819.6	677.1
Short Term Investments	130.0	160.0	-	320.0	320.0
Cash and bank balances	670.7	788.6	883.7	475.5	651.1
Long Term Loan	500.0	1,000.0	1,000.0	1,000.0	1,000.0
Total Assets	1,569.4	1,639.3	1,706.2	1,657.2	1,669.1
Creditors, Accrued & Other Liabilities	524.6	570.7	90.6	26.4	27.6
Lease Key Money	28.9	5.3	5.0	5.0	5.0
Total liabilities	553.5	576.2	96.2	32.1	35.7
Paid up Capital	450.0	450.0	450.0	450.0	450.0
Equity	1,015.8	1,063.0	1,610.0	1,625.1	1,633.4
INCOME STATEMENT	**FY18**	**FY19**	**FY20**	**FY21**	**9M'22**
Income from Diminishing Musharaka	55.0	92.4	101.9	79.0	66.7
Income from Ijarah financing	10.7	4.7	0.8	0.6	-
Income from Bank deposits	14.2	15.9	83.3	43.8	31.4
Term Deposit Receipts	8.4	12.0	2.1	14.8	17.5
Operating Expenses	28.9	32.1	39.2	46.4	30.2
Profit/ (Loss) Before Tax	52.4	81.2	107.6	75.8	75.2
Profit/ (Loss) After Tax	52.4	81.2	107.6	75.8	53.4
RATIO ANALYSIS	**FY18**	**FY19**	**FY20**	**FY21**	**9M'22**
Current Ratio (x)	2.0	2.1	12.2	37.4	37.64
Efficiency (%)	32.3%	25.6%	20.9%	33.6%	26.1%
Gross Infection (%)	0.5%	0.5%	4.0%	5.5%	6.8%
Gearing (x)	-	-	-	-	-
Leverage (x)	0.5	0.5	0.1	0.0	0.0
ROAA (%)	4.0%	5.1%	6.4%	4.6%	4.3%*
ROAE (%)	5.2%	7.8%	8.1%	4.7%	4.4%*

**annualized*

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: 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

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

(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

'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

Name of Rated Entity	Sindh Modaraba
Sector	Modaraba
Type of Relationship	Solicited
Purpose of Rating	Entity Rating
Rating History	
Instrument Structure	N/A
Statement by the Rating Team	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	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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Due Diligence Meetings Conducted	

Rating History:

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
RATING TYPE: ENTITY				
06/30/2022	A+	A-1	Stable	Reaffirmed
06/29/2021	A+	A-1	Stable	Reaffirmed
06/30/2020	A+	A-1	Stable	Reaffirmed
02/22/2019	A+	A-1	Stable	Reaffirmed
12/29/2017	A+	A-1	Stable	Reaffirmed
01/16/2017	A+	A-1	Stable	Initial

Due Diligence Meetings Conducted:

S. No	Name	Designation	Date
1	Mr. Adnan Shakeel	CFO & CS	June 14, 2022
2	Mr. Faraz-uz- Zafar	Head Compliance	June 14, 2022