

CREDIT RATING REPORT ON PHOENIX FINANCE AND INVESTMENTS LIMITED

REPORT: RR/103/07

Address:

Nakshi Homes (4th floor)
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Seginbagicha, Dhaka

This is a credit rating report on Phoenix Finance & Investments Limited as per the provisions of the Credit Rating Companies Rules 1996. CRISL long-term rating is valid for only one year and short term rating for six months. After the above periods, these ratings will not carry any validity unless the company goes for rating surveillance on voluntary basis.

	Long Term	Short Term
Entity Rating	A-	ST-3
Previous Rating	BBB	ST-4
Date of Rating	March 27, 2007	

Analysts:

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Entity Rating

Long term: A-
Short term: ST-3

PHOENIX FINANCE & INVESTMENTS LIMITED

PRINCIPAL ACTIVITY
Lease Financing

INCORPORATED ON
April 19, 1995

BOARD CHAIRMAN
Mr. Deen Mohammad

MANAGING DIRECTOR
Mr. A. Quadir Choudhury

EQUITY
TK. 397.19 Million

CREDIT PORTFOLIO
TK. 4472.54 million

1.0 RATIONALE

CRISL assigns A-(A minus) rating to Phoenix Finance and Investments Limited (hereinafter called PFIL) in the long run and ST-3 rating in the short-term. The above rating has been done on the basis of its good fundamentals such as diversified product line, wide geographical coverage, improving trend of asset quality and sound liquidity position. However, the above factors are outshined to some extent by moderate corporate governance, lower operating efficiency, high gearing ratio and inadequate credit & operational risk management tools. Financial Institutions rated in this category are adjudged to offer adequate safety for timely repayment of financial obligations. Risk factors are more variable and greater in periods of economic stress than those rated in the higher categories. Short term rating ST-3 indicates good certainty of timely payment. Liquidity factors and company fundamentals are sound. Although ongoing funding needs may enlarge total financing requirements, access to financial markets is good and risk factors are small.

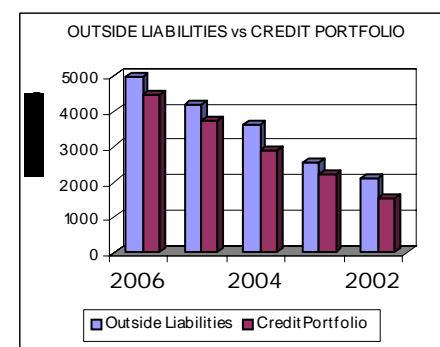
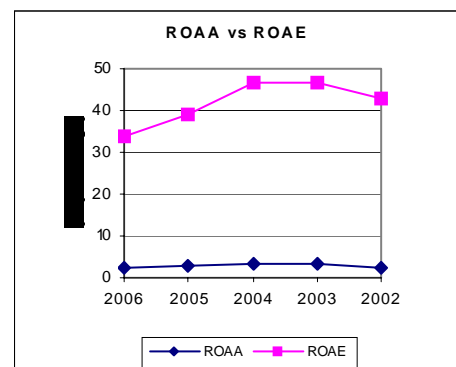
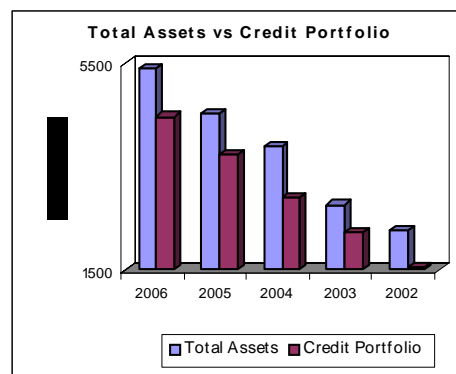
2.0 PREVIOUS RATINGS

CRISL assigned BBB (pronounced as triple "be") rating to Phoenix Finance & Investments Limited in the long term and ST-4 rating in the short term. The above had been done on the basis of its good fundamentals such as satisfactory market share, wide geographical coverage and satisfactory growth of earning assets. However, the above factors were constrained by below average asset quality, decreasing trend in financial performance, insufficient risk management tools, IT infrastructure at infant stage, limited product lines, etc.

3.0 CORPORATE PROFILE

3.1 The genesis

The Phoenix Finance & Investments Ltd. (PFIL) is a second generation Financial Institution in Bangladesh. PFIL, previously known as Phoenix Leasing Company Ltd.



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(PLC), was incorporated as a public limited company on April 19, 1995 under the Companies Act 1994 with the vision to act as the best financial service provider in the country. The company started its operation on May 09, 1995 by obtaining license from Bangladesh Bank under Financial Institutions Act 1993 with an authorized capital of Tk. 500.00 million which subsequently increased to TK. 1000 million constituting 10.00 million shares of Tk. 100 each. Recently, the company was renamed as Phoenix Finance & Investments Ltd. after obtaining approval from Bangladesh Bank. The PFIL has been sponsored mainly by an industrial group linked to different industrial sectors. The company achieved commendable asset growth during the last five years. The credit portfolio of the company stood at Tk. 4.47 billion as on December 31, 2006. The company expanded its business operation with wide geographical coverage in Dhaka, Chittagong, Khulna and Bogra holding stable market share. Major products of the company confined to funded products, which includes lease, term and house finance. Recently, PFIL opened a new branch for small and medium enterprise (SME) financing. The move of PFIL for Initial Public Offerings (IPO) will meet the need of additional capital requirement of Bangladesh Bank (BB) and it will dilute the existing share concentration.

Authorized capital increased to TK. 1000 million

3.2 Ownership Pattern

PFIL, a closely held public limited company, is an initiative of few institutions, industrialists and professionals. The company is entirely owned by domestic shareholders having 2,111,875 shares outstanding with paid up capital of TK. 211.18 million as on December 31, 2006. Under individual shareholdings, twenty nine shareholders are holding 80% share of the company of which Mr. Ahmed Rajeeb Samdani holds the highest share of 10.67% while Mr. Aziz- Al- Mahmood and the Chairman of the Board Mr. Deen Mohammad hold 8% and 7.60% shares respectively. Among the individual shareholders, six shareholders are holding more than 5% share, while eleven shareholders are holding less than 1% share. Under institutional shareholdings, Phoenix Insurance Co. Ltd., an associate company of the Chairman, Mr. Deen Mohammad, holds 20% share of the company. While analyzing the family shareholding pattern, it has been revealed that Mr. Deen Mohammad and his family members hold 16.77% shares. However, no other family group holds more than 10% shares. The above shareholding pattern of the company reveals relatively high concentration of ownership among few shareholders. However, after ensuing IPO floatation, the ownership will be diluted to a great extent.

Closely held public limited company

3.3 Market Share

PFIL is operating its business with stable market share. The credit portfolio of 28 FIs stood at Tk. 61.90 billion in 2005 whereas the share of the credit portfolio of PFIL stood at Tk. 3.73 billion, representing 6.03% market share. The growth of the credit portfolio is also in line with the industry growth. The outstanding credit portfolio of the company stood at TK. 4.47 billion as on December 31, 2006 with 19.83% growth rate compared to previous year. It is notable here that the growth of direct finance is higher than that of lease finance.

Stable market share

3.4 Product and Services

The product line of most of the financial institutions in Bangladesh is confined to lease and term financing. However, PFIL is getting out of the trend by expanding its credit line to real estate finance and home loans, work order finance, bridge finance, syndication finance, consumer durables, SME financing, attractive deposit schemes etc. The company has also a membership at Dhaka Stock Exchange (DSE) as broker. PFIL has a plan to expand its activities as Merchant Banker and Off-shore Financer in near future.

Diversified product line

4.0 FINANCIAL INSTITUTION SECTOR

Financial sector of Bangladesh had long been solely confined to banking since its independence. However, with the promulgation of Financial Institutions Act 1993, the sector has entered into a new era of development, which gave rise to 22 leasing companies in the last 12 years. In addition, there are four (4) Development Financial Institutions and three (3) House Building Finance Companies operating in the country. Alongside banks, leasing companies have been contributing significantly in the country's trade and commerce, housing, transportation and in the information technology in the preceding years of operation. The central bank of Bangladesh (Bangladesh Bank) is entrusted with the power to supervise the operation of the FIs. Over the last decade, this sector witnessed a number of changes which eventually made their operation more effective and consolidated. Bangladesh Bank, in its effort to streamline the activities of the financial institutions, enacted the loan classification and provisioning system as a mandatory task for all the companies since the year 2000. Transformation into financial lease method in 2004 from the operating lease method of accounting is another development of the sector that reduces the confusion between

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lessor and the lessee, and brings fair presentation in the accounting treatment.

Market size of credit portfolio of the above FIs was Tk. 61.90 billion as on 31st December 2005. Along with the banks, FIs enjoy the privilege of issuing shares, debentures and bonds to raise funds. They are allowed to deal with public deposits and to borrow funds from banks under the Financial Institutions Act 1993. Along with lease financing, FIs are also allowed to participate at the money market with some ceiling based on capital. However, with the opening of leasing units by the banks directly, financial institutions have been facing tough competition. In addition, Government has increased corporate tax from 40% to 45% for the financial institutions, which has reduced the after tax profit margin of the above institutions.

5.0 CORPORATE GOVERNANCE

Moderate corporate governance

Governance is becoming a deciding factor of corporate management in recent days although it has been playing vital role in corporate management. Corporate governance is a blend of law, regulations, enforcement and appropriate voluntary practices by the companies that permit a corporate to attract capital, perform efficiently and generate long term economic value for its shareholders while respecting the interest of its stakeholders and society as a whole. The specific areas covered are transparency in disclosure of relevant reliable financial and operational information, information on ownership and control, information on internal processing of management. PFIL is functioning with moderate corporate governance practices. In pursuit of the above facts, CRISL examines and evaluates the following:

5.1 The Board of Directors

Board involves with policy issues

The Board of PFIL consists of eleven directors including nine individual Directors and two representative Directors from Phoenix Insurance Co. Ltd. Mr. Deen Mohammad, as mentioned earlier, is the Chairman of the Board. He is a leading businessman, industrialist, pioneer personality & entrepreneur of private sector banks in Bangladesh. The Chairman himself and two other Directors from his family jointly hold 12.33% shares. Besides, Prof. Dr. Ali Afzal Khan, another director of the Board holds 7% shares of the company. The Board members jointly hold 48.25% shares of the company under different capacity. The Board held 11 meetings each during the year 2004, 2005 and 2006. The Board is involved with policy issues and reviews the performances of the company through moderate business and limited financial delegation to the operating management. The Directors take part in the Board meetings regularly.

5.2 Committees

Chairman of the Board is the Chairman of EC

The Board has a six members Executive Committee (EC) headed by Mr. Deen Mohammad who is also the Chairman of the Board. In best corporate practice the Chairman of EC and the Chairman of the Board should be different person. The EC enjoys specific power delegation for business and non-business activities of the company. EC can approve credit proposals up-to Tk.5 million, which is considered to be poor delegation of financial power to the Committee. However, the Board delegated expenditure sanctioning power of the EC to Tk. up-to TK.0.50 million. The Board also formed a five member Management Audit Committee and a five member Risk Management Committee respectively under the Chairmanship of Mr. M. Yunus and Mr. Mohammed Shoeb respectively who are directors of the company. Other members of the above two Committees are the senior professionals. The Audit Committee is responsible for the smooth operation and effective control of the company while the Risk Management Committee is responsible for assessing and identifying the probable sources of risks and exploring the defense mechanism to minimize them.

5.3 Management

The management team of the company is headed by Mr. A Quadir Choudhury who joined the company as founder Managing Director after his voluntary retirement from Agrani Bank in 1995. In his long career, he served in many important positions in different banking and financial institutions under different capacities since 1965. It is mentionable here that Mr. Choudhury is also a Director of the Board as sponsor shareholder with 0.50% share. In the management team, MD is aided by one Executive Vice President (EVP), one Senior Vice President (SVP), three Vice Presidents (VP) and nine Assistant Vice Presidents (AVP). However, the company has the plan to recruit a Deputy Managing Director (DMD) soon in line with having a well succession plan. The activities of the company are being operated mainly under Operations & Marketing (O & M) and Finance & Accounts (F & A) Department. The O & M department is headed by the SVP while F & A Department is headed by a VP. In addition, the company has Internal Audit Department, Law and Recovery Department, IT department and Human Resource Department. The company has four branches (including its newly opened SME branch) at Dhaka, Chittagong, Khulna and Bogra. However, the branch activities are regularly supervised by the respective department of Head Office.

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*Satisfactory human
resources quality*

5.4 Human Resources Management

PFIL has an experienced management team with wide exposure in different financial institutions. The quality of human resources is found to be satisfactory. The company has its documented Service Rules for the employees to create congenial working environment. The compensation package found average among the peer Financial Institutions. Human Resources activities are supervised by an AVP. The company has sufficient staffs in different tiers of management. The total Human Resource strength of the company is 70 including 16 supporting staffs as on December 31, 2006. It is notable here that human resources turnover rate sharply declined to 6.78% in 2006 against 21.28% in 2005. Top level executives were immediately replaced during 2006. While the Human resources development activities of the company are improving, the company still has no separate in-house training wing. During the year 2006, total 23 different level executives attended in different training program in different outside organizations. The training programs were related to internal control management, compensation management, customer and vat management, corporate governance, credit risk management, bank and Financial Institutions rating and other different foundation and professional courses.

MIS at initial stage

5.5 Management Information System

The Management Information system of the company is at the initial stage. The company placed work-order to introduce integrated software named "FIntelligent" which is under implementation and expected to be in full-fledged operation from April, 2007. Presently, inputs of both financial and other information of various departments are being made in the Fintelligent software side by side with Tally software and MIS reports are being generated by using MS Office to meet the regulatory compliance and management requirement. The company uses 60 desktop computers connected with Local Area Network (LAN) supported by three servers. However, the branches are yet to be connected with Wide Area Network (WAN). The IT related activities of the company are being conducted by the head of IT (in the rank of PO) with two data entry operators under direct guidance and supervision of the SVP.

5.6 Best practice guideline of Corporate Governance

The PFIL is still a closely held public limited company. The composition of the Board, formation of management structure, style of management, disclosures etc are all based on ownership criterion. However, after flotation of IPO, the company may or should follow the minimum requirements of Securities & Exchange Commission corporate governance guideline. The company needs to have at least one Independent Director in the Board and a Board Audit Committee with at least three directors including one Independent Director. In addition the company will be required to have a Chief Finance officer, Internal Auditor and a Company Secretary. The company Secretary is to work as the Compliance Officer. Since the PFIL is required to go for public offering of shares, this minimum corporate governance guideline will be required to be followed by "comply or explain" basis. However, the company already appointed a Company Secretary, a Vice President (to work as Chief Finance Officer) and one Internal Auditor.

*Company has the
philosophy to retain its
client base*

6.0 Marketing Strategy

The marketing aspects of the company are carried out by Operation & Marketing (O & M) Dept. The department comprised of 19 professionals under the direct supervision of an SVP. Management expects that the above team will assist the company to achieve its desired business target. In addition, PFIL has a Law and Recovery Department to look after legal and recovery aspects of the company. Generally, clients are selected by the initiatives of the Relationship Managers (RM) and the company has the philosophy to retain its existing clients based on their performance. However, the company need to have comprehensive marketing plan for their future operations.

Recently, PFIL opened a new branch which will be dedicated for small and medium enterprise (SME) financing. The company formulated detailed policy for credit facility to SME financing that has been approved by the Board. CRISL believes that the endeavor of PFIL will assist to enhance its market share. In addition, PFIL is pondering to diversify resource-mix by floating 5 years' bond in the market to mobilize TK. 200 million in year 2007. The company will continue to enhance its deposit base through launching more attractive deposit products and expanding branch network.

7.0 PERFORMANCE

*Average financial
performance*

7.1 Financial Performance

Financial performance of PFIL is found average compared to its peer. The company reported profit after tax of TK. 78.68 million in 2006 against TK.66.24 million in 2005 with a growth rate of 18.78%. However, total earning assets of the company has increased by 19.36% in 2006.

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Remarkable growth in income from direct finance

The growth of operating revenue of the company in 2006 stood 37.51% which is the highest compared to previous years of operation. The company experienced remarkable growth in income from direct finance in 2006. However, operating expense of the company increased by 45.63% in 2006, which is mainly because of increased financial cost and direct administrative expenses. The reason behind this high financial burden was mainly due to relatively high interest bearing term deposits and term loan because of market pressure. It has been revealed that term deposits of the company has increased to TK.2638.93 million as on December 31, 2006, about 50% of which is public deposit representing increased public confidence on the company.

While analyzing the income composition, it has been observed that lease income hold the highest portion of 57.63% of total operating revenue while direct finance contributes 15.28% as on December 31, 2006. However, a substantial amount (25.73%) of operating income generated from the realization of IDCP and delinquency charges.

The financial performance in terms of return on average equity stood at 33.64% which was in line with the peer, although the same has decreased in terms of percentage over the previous year. The earning per share (basic) of the company stood at TK.37.26 in 2006 although the Peer median of 2005 was quite high. The return on average earning asset as on December 31 2006 stood at 2.36% against 2.61% in the previous year and 3.80% peer median at year end 2005. Again, net assets value per share of TK. 100 has slightly reduced to TK.188.07 in 2006 compared to TK. 188.53 in 2005 due to increase in share capital.

7.2 Operating Efficiency

Lower operating efficiency

The operating efficiency ratios of PFIL are at lower end compared to its peer. The operating income of PFIL in 2006 stood at Tk. 717.55 million against operating expense of Tk.601.54 million representing operating profit of Tk. 116.01 million. Net profit margin (NPM) decreased to 10.96% in 2006 from 12.69% in 2005 which was found much lower than that of peer median.

Efficiency related ratios of PFIL also showed a declining trend. Efficiency ratio (cost to income) of the company raised to 83.83% as on December 31, 2006 compared to 79.16% in 2005 against its peer median of 73.77% in 2005. Again, general and administrative expense to average earning assets slightly declined to 1.52% in 2006 compared to 1.58% in 2005 against peer median of 0.97% in 2005. The company is earning lower staff yield compared to its peer median. The yield per Tk. staff cost also decreased to Tk. 3.27 in 2006 from Tk. 4.03 in 2005 against its peer median of Tk. 10.23 in 2005.

8.0 RISK MANAGEMENT

Risk management is one of the core operational pillars of financial institutions. The primary objective of risk management is to take calculative risk in order to safeguard its capital and well managed financing business. In order to go for more risk sensitive financing, Bangladesh Bank formulated Core Risk Management Guidelines on the basis of best practices in the industry and advised the FIs to comply with the above. The risk management modules circulated by the Bangladesh Bank covers 3 (three) core risk areas i.e. credit risk, asset and liability/balance sheet risks, internal control and compliance risks. CRISL has reviewed the RISK management of the company as delineated below:

8.1 Credit Risk Management

Traditional credit risk management tools

PFIL operates its financing activities without having sufficient credit risk management tools. However, the company formulated procedures for risk management which are yet to be executed. Ideal credit process includes Credit Marketing, Credit Analysis and Credit Administration. The above activities need to be separated for effective credit risk management, which is yet to be ensured in the company. PFIL is yet to be stepped to adopt credit risk grading system at the pre-sanction stage for proper transparency in credit management which will ensure the lending price, extent of exposure, appropriate credit facility or lending decisions to any client. On the contrary, the company still follows traditional Lending Risk Analysis (LRA) for evaluating the credit worthiness of the borrower.

The company follows Bangladesh Bank rescheduling or restructuring policy. The credit portfolio is diversified into different sectors; however sector-wise allocation of credit is being made annually with the approval of Executive Committee/ Board of Directors. PFIL recently formed a full-fledged Special Recovery Squad headed by a retired Army officer apart from its existing recovery dept.

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The above policy enables the company to improve its asset quality. The company follows Bangladesh Bank (BB) guideline in loan loss provisioning and keeps provision in accordance with the above.

Traditional credit appraisal policy

8.1.1 Credit Approval Process

PFIL follows a traditional credit appraisal policy. Operation & marketing Department (O & M) is responsible for all credit related function. Each credit file is handled by one assigned Relationship Manager (RM) who is responsible for soliciting new businesses and preparing credit proposals, and subsequently forwards to the Operation Department. Operation Department, along with the participation of RM, reviews the proposals, validates the assumptions and security covenants requirements and recommends to the Managing Director. Finally, Managing Director forwards the same with recommendation to Executive Committee (EC) or the Board for final approval as per the delegation of power. It is worth mentionable here that there is no delegation to management team to approve any proposal except recommendation. Executive Committee can approve up-to Tk. 5 million while the Board can approve any limit up to 30% of PFIL's equity.

Inadequate operational risk management tools

8.2 Operational Risk Management

The operational risk is defined as the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events. Some of the examples of Operational Risks are internal and external frauds, legal risks, damages to clients, diversity, damage to physical assets, business interruptions etc. The global best practice suggests that the financial institutions irrespective of size and business must identify and assess all operational risk against all of its products and services and monitor the same through an operationally independent professional.

Operational risks are primarily managed by Operations and Finance & Accounts Departments without having any standardized operational risk management tools. The company has a five member Audit Committee and recently formed a one member internal audit department. However, these efforts are yet to make any breakthrough of traditional system for internal control. The respective departments of the Head Office supervise the overall activities of branch offices. The branches do not have any financial delegation rather Head office approves all financing proposals of all the branches. All expense vouchers of branches and head office are verified by the Head Office authority. The company developed a Product Policy Guideline (PPG) which was subsequently approved by the Board. CRISL believes that the company can improve its internal control mechanism through efficient implementation of the above guideline. For the data protection system, the company keeps adequate backups in the server on daily basis. The company secretary supervises internal and external compliance issues with different stakeholders.

Planned asset-liability management

8.3 Assets-Liabilities Mismatch Risk

PFIL has been operating with an Asset-Liability Management Committee (ALCO) comprising of the Managing Director, Head of Treasury, Head of Operation and Head of Finance & Accounts. The committee is responsible for looking after the money market activities, managing liquidity and interest rate risk, understanding the market position and competition and reviewing on the interest rate structure. The committee does not hold any formal meeting, yet meets on regular basis.

While analyzing the maturity structure, no significant maturity gap was found in any long term maturity bucket rather the company has sufficient assets backup position. However, the company has TK. 489.23 million and Tk. 69.39 million net liquidity differences (negative) respectively in 6 months-1 year and 3-6 months bucket which apparently reveals short term liquidity crisis. Nevertheless, while analyzing the components of these buckets, it has been found that term deposits from different financial institutions constitute the lion's share of liabilities of these buckets which are subject to renewal, thus minimizes the risk.

8.4 Financial Risk

The income tax rate applicable for FIs is 45% on the net profit before tax (NPBT). The leasing companies having the ownership title of the lease assets are entitled to practice accelerated/initial depreciation as per NBR rules. Since the accounting depreciation covers a wider accounting period compared to the accelerated/initial depreciation period, the leasing companies are getting a time difference to temporarily defer their tax liabilities by availing accelerated depreciation / initial depreciation. In that case, the companies are required to provide for deferred taxes under BAS 12 to avoid future extra tax burden against the lease portfolio and to match the tax burden with the income. PFIL has been enjoying accelerated/initial depreciation against the assets of its portfolio and has provided for deferred tax.

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Tk. 41.69 million tax provision during 2006

The outstanding provision for taxation of the company stood TK.93.71 million as on December 31, 2006. During the year 2006, the company made TK. 41.69 million tax provision against net profit before tax of TK.120.37 million. However, tax liability is yet to be determined as on the reporting date and subsequent adjustment is required. With the above policy, the company has been carrying some financial risk. In order to avoid any substantial income tax/ financial risk PFIL, like most of its peer companies, is providing substantial amount of deferred tax in the financial statements.

Higher end of interest rate risk

8.5 Interest Rate Risk

Financial market of Bangladesh has been experiencing volatile interest rate in recent years. Pressure of market to reduce the lending rate forced the FIs to rearrange interest rate of financing agreements in many cases, which ultimately squeezed the margin of FIs. However, recently interest rate has been moving up again. Subsequent interest rate adjustment capability of the company plays a vital role in minimizing the interest rate risk. PFIL has a clause in its credit agreement of necessary interest rate adjustment in accordance with the market pressure, which provides flexibilities to the company to adjust interest rate. Funding composition as on December 31, 2006 shows that the company has arranged 59.18% of the total fund from different Financial Institutions and 24.42% through public borrowing; therefore, the company is in the higher end of the interest rate risk.

9.0 ASSET QUALITY

The total assets footing of PFIL was worth of TK. 5,394.83 million as on December 31, 2006. Of the above, 65.01% was lease assets and 17.89% was composed of direct finance while the balance was consisted of cash and cash equivalent and other assets. CRISL has reviewed the above assets as follows:

Improving trend of asset quality

9.1 Quality of Credit Portfolio

The asset quality of PFIL is found good and showing an improving trend. FICL statement submitted to Bangladesh Bank as on December 31, 2006 reveals classified amount of Tk. 74.40 million indicating a substantial reduction of non-performing loan (NPL) compared to that of June 30, 2006. The gross NPL ratio of the company stood at 1.86% as on December 31, 2006 compared to that of 3.19% on June 30, 2006. After considering provision and interest suspense, the net NPL ratio stood at 0.77% as on December 31, 2006 against 1.61% in June 30, 2006. The gross NPL coverage ratio also improved to 119.66% as on December 31, 2006 against 87.91% in June 30, 2006. The above performance has been achieved through PFIL's deliberate efforts for collection and monitoring. However, infection ratio (considering overdue of one and above) of the company stood at 40.88% as on December 31, 2006 showing no significant improvement compared to that of previous year. It has also been identified that risk prone assets (overdue of three and above) constitute only 5.76% of the total outstanding, indicating the lion's share of the infected assets lounge within overdue of two installments. In addition, it has been identified that high risk prone assets (overdue for 5 installments) in the portfolio reduced to 1.25%, indicating further deteriorating possibilities of this portfolio to NPL within a month. While analyzing the sector-wise asset quality it has been observed that lease finance infection ratio constitutes the highest of 48.33% followed by 28.87% and 8.61% respectively in house finance and term finance.

1.86% Gross NPL

The total outstanding credit portfolio of top 20 contracts (on outstanding basis) of PFIL stood at TK.1256.63 million which holds 31.49% of total credit portfolio as on December 31, 2006. It has been revealed that out of these contracts six contracts have been rescheduled of which three contracts have been rescheduled for the second time. The infection ratio of these contracts was 25.14%.

Chittagong and Bogra Branches maintain better asset quality

9.2 Branch-wise Asset Quality

While analyzing asset quality at branch level it has been found that Chittagong and Bogra Branches are maintaining better asset quality compared to head office and Khulna branch. It is worth mentionable that the asset quality (in terms of infection) of Khulna branch is the highest with 94.38% infection ratio even though the branch constitutes only 2.59% of total contracts. The assets infection ratio of Head Office is 43.03% as on FICL December 31, 2006 constituting 82.70% of the total contracts of which 52.96% contracts found infected. The asset quality of Bogra branch found good with only 13.49% infection ratio, however, the operation of this branch is yet to be expanded. In terms of classification status it has been found that head office constitutes 96.80% of the total non-performing loan while the remaining 3.20% by the Chittagong branch without having any NPL in other two branches.

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Average large loan exposure

9.3 Large Loan Exposure

Large loan exposure of the company found to be average. Large loan (equal or above TK. 50 million) was TK. 924.99 million (on outstanding basis) with infection ratio of 20.39% in accordance with the FICL statement submitted to Bangladesh Bank as on December 31, 2006, representing 23.18% of the total outstanding amount. However, head office holds the lion's share (85.18%) of the total large loan exposure. While analyzing the performance of the large loan, no non-performing loan was found, however, five contracts have been rescheduled (including three contracts rescheduled for twice) of which two contracts have been found infected.

Keeps required provision for infected investment portfolio

9.4 Quality of Investment Portfolio

The investment portfolio of PFIL in different securities stood at TK. 55.01 million (on acquisition cost) as on December 31, 2006 consisting of Tk. 16.77 million in primary shares and Tk.38.24 million in secondary shares. While analyzing the market price of the investment portfolio it has been observed that the market price of primary shares decreased to Tk.10.07 million while secondary shares increased to Tk. 66.18 million representing a net gain of Tk.21.24 million. However, the company charged Tk. 7.44 million provision during this period.

Poor performance of rescheduled assets

9.5 Performance of Rescheduled Assets

Performance of the PFIL's rescheduled assets is poor. The outstanding amount of rescheduled assets of the company stood at TK. 980.60 million as on December 31, 2006 against 119 contracts of which 22 contracts have been rescheduled for the second time. The above rescheduled amount represents 24.57% of the total outstanding amount. While analyzing the performance of the rescheduled assets it has been found that 49.41% of the outstanding rescheduled assets have been infected after rescheduling, 95.36% of which is lease assets.

Transport sector considered to be high risky

9.6 Sectoral Exposure

The credit portfolio of PFIL is diversified into different sectors. Textile sector holds the highest share of 30.68% of the total credit portfolio followed by service, garments & accessories and transport sector of 12.44%, 9.74% and 9.37% as on December 31, 2006. While analyzing the loan classification status it has been revealed that transport sector constitutes 42.06% of the total classified loan which is considered to be high risky sector. It is worth mentionable here that information & technology sector represents 14.17% of the classified loan against only 1% of the total outstanding credit portfolio.

TK. 31.07 million related party transaction

9.7 Related Party Transactions

The related party transaction of the company is TK. 31.07 million (on receivable basis) against 17 lease/ loan contracts under personal and corporate guarantee, of which most of the lease assets are backed by their ownership title in the name of the company. According to the quarterly lease/loan statement of related parties submitted to Bangladesh Bank, the overdue amount stood at TK.1.61 million as on December 31, 2006, however all the contracts found unclassified.

10.0 CAPITAL ADEQUACY

Relatively inadequate capital base

PFIL is operating with relatively inadequate capital base compared to its peer. Almost all the capital adequacy related ratios also showed weaker position in the peer companies in 2005, yet the position to some extent improved in 2006. Nevertheless, recent move of the company to issue IPO (Initial Public offering) to fulfill the capital adequacy requirement of Bangladesh Bank will enhance its capital base. Shareholders equity of the company stood at TK. 397.19 million as on December 31, 2006 which includes share capital of TK. 211.19 million and reserves and surplus of TK. 186.00 million.

Shareholders' equity to total assets was 7.03% during 2005 against peer median of 9.34% representing lower equity back-up of the assets which slightly improved to 7.36% as on December 31, 2006. Again, credit portfolio to shareholders equity has fallen to 11.26 times in 2006 against 11.72 times in 2005 which is much higher than peer median of 6.66 times in 2005. Total gearing ratio found higher (13.23 times) compared to peer median (9.72 times) in 2005 indicating lower equity back-up against outside source of fund. However, the ratio declined to 12.58 times in 2006. Internal capital generation of the company was 23.21% compared to its peer median of 22.92% in 2005; however the same has reduced to 7.23% in 2006 due to proposed cash dividend of Tk.52.80 million during the period.

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11.0 FUNDING AND LIQUIDITY

11.1 Fund Management

PFIL is operating with sufficient funding sources. The funding sources include term loan, term deposits (both institutional and public), call loan and promissory notes. The total asset base of TK. 5394.83 million as on December 31, 2006 of PFIL was financed by shareholders' equity of 7.36%, long term loan of 28.17%, term deposit of 48.92%, call loan of 6.49% and other liabilities and provisions of 9.06%.

Sufficient funding sources

Finance and Accounts department has been looking after the fund management. PFIL is enjoying funded facility from 16 different banks including Bangladesh Bank. As on December 31, 2006 the credit lines availed from different banks stood TK. 1871.15 million of which term loan was TK.1519.903 million, short term loan & SOD was TK.1.25 million and call loan was TK.350 million. The company regularly involved in call operation during 2006 with an average borrowing of TK. 51.14 million per day within the range of 8% to 28% interest rate. PFIL has significant investment in FDR in different commercial banks @10.75% (average) interest rate and the company, in times of need, takes overdraft facility @12.75% (average) against the above FDRs as lien. Though the company is facing a margin loss of 2%, this has been done to maintain the financial flexibility.

11.2 Liquidity Management

The company has been operating its financing activities under sound liquidity position during the last couple of years. Almost all the liquidity indicators of the company showed above peer median in 2005. Current ratio of the company was 1.89 times in 2006 compared to 1.91 times in 2005 against peer median of 1.15 times. Liquid assets to current liabilities ratio stood at 0.34 times in 2006 compared to 0.32 times in 2005 which is much higher than that of its peer median. Time interest earned ratio of the company reduced to 1.27 times in 2006 against 1.38 times in 2005 due to increased financial burden during the period, however, the position of the company found to be in line with the peer companies. Loan (credit portfolio) to deposit ratio slightly decreased to 1.69 times in 2006 from 1.76 times in 2005, though there is no guideline regarding this ratio for FIs.

Sound liquidity position

12.0 SWOC ANALYSIS

<p>Strengths:</p> <ul style="list-style-type: none"> <input type="checkbox"/> Wide geographical coverage <input type="checkbox"/> Product diversification <input type="checkbox"/> Improving trend of asset quality <input type="checkbox"/> Sound liquidity position 	<p>Weaknesses:</p> <ul style="list-style-type: none"> <input type="checkbox"/> Moderate corporate governance <input type="checkbox"/> Lower operating efficiency <input type="checkbox"/> Inadequate operational and credit risk management tools <input type="checkbox"/> Highly leveraged
<p>Opportunities:</p> <ul style="list-style-type: none"> <input type="checkbox"/> Scope to explore fee based products <input type="checkbox"/> Scope of exploring cheaper sources of fund 	<p>Challenges:</p> <ul style="list-style-type: none"> <input type="checkbox"/> Increased competition in the market for quality products <input type="checkbox"/> Commercial banks portfolio expansion to lease financing <input type="checkbox"/> Increasing competition compelling reduction in rental rate

13.0 PROSPECTS

The business prospects of the FIs particularly depend on the stable macroeconomic fundamentals of the country. Despite the impact of higher oil prices and the end of textile and clothing quotas, the development outlook remains broadly positive. After reviewing the favorable state of the economy, the Government and development partners envisage a 6% to 6.5% GDP growth in the fiscal year 2006-07 which is still, however, lower than the 7%, required to achieve the Millennium Development Goals.

Inflationary pressures will persist, as monetary policy is set to remain broadly accommodative so as to support strong credit demand and economic expansion. Although the trade deficit will widen, pressures on the balance of payments are expected to remain at a manageable level, aided by strong remittance inflows. Major development challenges need to be tackled if investment is to be stepped up to move the country onto the higher growth path required for rapid poverty reduction-including substantial improvements to infrastructure, public policy, and governance. Based on the positive macroeconomic outlook, it is presumed to have strong growth potential of industry and

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service sectors which will offer PFIL with increased financing opportunities along with other financial institutions.

Though macroeconomic forecasts looks promising, the financial industry of Bangladesh is heavily fragmented, with too many banks and FIs (49 banks and 29 FIs) operating in a small economy like Bangladesh. Consequently, the institutions are locked in tough competition to secure market share. On the other hand, the Government increased corporate tax rate to 45% in FY 2002-03 for the financial institutions. Introducing Basel II by Bank of International Settlement (BIS) regarding capital adequacy on the basis of either Standardized Approach (SA) or Internal Rating Based (IRB) approach will remove the present practice of 20% risk weight of financing in financial institutions by the banks. The above capital adequacy advantage of the banks to finance in financial institutions including FIs will reshuffle the exposure according to the rating of the respective institutions. This may decrease the present practice of wholesale funding through banking sector to FIs, unless the FIs carry high investment grade rating. Therefore, extraction of funds from banking system will be dependent on the overall performance (and credit ratings) of the FIs. BB has already introduced mandatory credit rating for scheduled banks.

Presently FIs are allowed to deal with public term deposits and to borrow fund from the Financial Institutions. Along with lease financing FIs are also allowed to extend short and long term direct finance and to enjoy the privilege of issuing shares, debentures and bonds to raise funds. Under the above backdrop, the business volume of the FIs is in ascending trend along with their credit portfolios. However, its viability and sustainable progress depend on timely management action to properly address the weaknesses and to tap growth opportunities.

END

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CREDIT RATING REPORT ON PHOENIX FINANCE AND INVESTMENTS LIMITED

14.0 CORPORATE INFORMATION:

Date of Incorporation: April 19, 1995
Date of Commencement of Business: April 19, 1995

Board of Directors:

Mr. Deen Mohammad	Chairman
Mr. M. Yunus	Vice Chairman
Mr. Mohammad Shoeb	Vice Chairman
Mr. Wasef Ahamed	Representative Director from Phoenix Insurance Co. Ltd.
Mrs. Sadia Anjum Siddiqui	Representative Director from Phoenix Insurance Co. Ltd.
Mr. M. A. Majid	Director
Prof. Dr. Ali Afzal Khan	Director
Mr. Rafiqul Islam Khan	Director
Ms. Evana Fahmida Mohammad	Director
Mr. A. Quadir Choudhury	Director
Ms. Selina Akhter	Director

Auditor:

Zoha Zaman Kabir Rashid & Co Chartered Accountants

Management:

Mr. A. Quadir Choudhury	Managing Director
Mr. M Shah Alam	Executive Vice President
Mr. Ali Md. Masud	Senior Vice President
Mr. Md. Sayduzzaman	Vice President
Mr. Ahmed Reza Chowdhury	Vice President & Company Secretary
Mr. Razzaque Chowdhury	Vice President & Branch In-charge (Chittagong)
Mr. Faisal Hasan	Assistant Vice President
Mr. Md. Abu Sukkur	Assistant Vice President
Ms. Rebeka Akhter	Assistant Vice President
Ms. Shireen Akhter Karim	Assistant Vice President
Mr. Masud Kabir	Assistant Vice President
Mr. Rotom Ali Mollah	Assistant Vice President
Mr. Md. Badrul Haque Patwary	Assistant Vice President
Mr. Golam Kader	Assistant Vice President
Mr. Alhaj Ahmed Ali	Assistant Vice President & Branch In-charge (Khulna)

Capital History:

Year	Authorized Capital (Million Taka)	Issued, Subscribed and Paid-up Capital (Million Taka)	Rate of Increase %	Source of Capital
2003	500.00	105.00	-	
2004	500.00	136.25	29.76	Issuance of right and bonus share
2005	500.00	168.95	24.00	Issuance of bonus share
2006	1000.00	211.18	25.00	Issue of Stock Dividend

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FINANCIALS:

Balance Sheet

Tk in Million

Particulars	2006	2005	2004
Net fixed assets	121.56	102.20	78.95
Fixed assets-at cost	163.43	128.67	92.64
Depreciation	41.87	26.46	13.69
Lease assets:	2,533.89	2,211.13	2,306.82
Lease receivable (net of current maturity)	1,932.29	1,730.88	1,761.56
Advance against leasing assets	601.60	480.25	545.25
Direct Finance:	442.26	295.05	253.85
Term finance	80.40	136.94	131.17
House Building Finance	361.86	158.12	122.67
Investment in share (Net of current maturity)	47.56	44.08	14.79
Other Non- Current Assets	10.52	11.29	8.60
Provision for Doubtful Accounts:	(79.86)	(53.37)	(39.04)
Current Assets:	2,318.89	1,923.47	1,260.24
Accounts receivable	322.00	352.55	252.92
Advance, Deposits and Prepayment	77.44	23.02	34.09
Cash in hand and Banks	89.28	106.10	113.70
Fixed deposit receipt	333.78	175.50	507.74
Current maturity of investment in lease	973.28	861.87	145.42
Current maturity of Term & House finance	523.10	364.42	206.37
Investment in Call Loan	-	40.00	-
Total Assets	5,394.83	4,533.85	3,884.20
Shareholders' Equity :	397.19	318.52	252.28
Share capital	211.19	168.95	136.25
Reserves and Surplus	186.01	149.57	116.03
Long Term Liability -net of current maturity:	3,732.95	3,186.92	2,558.12
Long term loans	992.00	966.71	534.72
Advances	58.10	36.99	89.95
Security and other deposits	36.66	49.12	21.63
Term Deposits Receipt	2,638.93	2,123.43	1,895.75
Promissory notes	7.25	10.67	16.06
Other Non -Current Liabilities:	36.02	21.59	11.62
Deferred liability	22.85	14.13	-
Interest Suspense	13.17	7.46	11.62
Current Liabilities and Provisions:	1,228.66	1,006.83	1,062.19
Current maturity of term loans	527.90	488.54	150.85
Current Maturity of advance and security deposits	42.86	67.70	20.06
Short term loans	1.25	100.61	710.00
Payable and accrued expenses	212.93	154.79	134.30
Provision for taxation	93.71	60.17	46.98
Over Draft	0.003	0.02	-
Call Loan	350.00	135.00	-
Total Liabilities and Owners' Equity	5,394.83	4,533.85	3,884.20

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Income Statement

Particulars	2006	2005	2004
Total Operational Revenue:	717.55	521.83	406.99
Lease interest income	413.55	331.68	262.12
Income from term finance	34.67	18.37	-
Income from short term finance	45.56	19.41	-
Income from house finance	29.37	19.60	-
Other operational income	194.39	132.76	145.03
Total Operating Expense:	601.54	413.07	313.23
Salary and allowances	35.45	27.00	14.55
Depreciation of fixed assets	16.11	12.78	5.94
Other administrative expense	23.42	25.83	22.09
Financial expenses	499.99	326.03	258.47
Provision for bad & doubtful debt	26.50	14.32	8.28
Provision for investment in shares	0.08	7.12	-
Other operating expenses	-	-	3.88
Operating Profit	116.00	108.76	93.76
Non-Operational Income	4.36	3.28	10.63
Profit before tax	120.37	112.04	104.39
Provision for taxation	41.69	45.80	53.78
Profit after tax	78.68	66.24	50.62

CREDIT RATING REPORT ON PHOENIX FINANCE AND INVESTMENTS LIMITED

CRISL RATING SCALES AND DEFINITIONS

LONG TERM RATINGS

RATING	DEFINITION
AAA Triple A (Highest Safety)	Financial Institutions rated in this category are adjudged to be of best quality, offer highest safety and have highest credit quality. Risk factors are negligible and risk free, nearest to risk free Government bonds and securities. Changing economic circumstances are unlikely to have any serious impact on this category.
AA+, AA, AA- (Double A) (High Safety)	Financial Institutions rated in this category are adjudged to be of high quality, offer higher safety and have high credit quality. This level of rating indicates a corporate entity with a sound credit profile and without significant problems. Risks are modest and may vary slightly from time to time because of economic conditions.
A+, A, A- Single A (Adequate Safety)	Financial Institutions rated in this category are adjudged to offer adequate safety for timely repayment of financial obligations. This level of rating indicates a corporate entity with an adequate credit profile. Risk factors are more variable and greater in periods of economic stress than those rated in the higher categories.
BBB+, BBB, BBB- Triple B (Moderate Safety)	Financial Institutions rated in this category are adjudged to offer moderate degree of safety for timely repayment of financial obligations. This level of rating indicates that a Financial Institution is under-performing in some areas. Risk factors are more variable in periods of economic stress than those rated in the higher categories. These entities are however considered to have the capability to overcome the above-mentioned limitations.
BB+, BB, BB- Double B (Inadequate Safety)	Financial Institutions rated in this category are adjudged to lack key protection factors, which results in an inadequate safety. This level of rating indicates a Financial Institution as below investment grade but deemed likely to meet obligations when due. Overall quality may move up or down frequently within this category.
B+, B, B- Single B (High Risk)	Financial Institutions rated in this category are adjudged to be with high risk. Timely repayment of financial obligations is impaired by serious problems which the entity is faced with. Whilst an entity rated in this category might be currently meeting obligations in time, continuance of this would depend upon favorable economic conditions or on some degree of external support.
C (Very High Risk)	Financial Institutions rated in this category are adjudged to be with very high risk of timely repayment of financial obligations. This level of rating indicates entities with very serious problems and unless external support is provided, they would be unable to meet obligations in a timely fashion.
D (Default)	Financial Institutions rated in this category are adjudged to be either currently in default or expected to be in default. This level of rating indicates that the entities are unlikely to meet maturing financial obligations and calls for immediate external support of a high order.

SHORT TERM RATINGS

ST-1	Highest Grade Highest certainty of timely payment. Short-term liquidity including internal fund generation is very strong and access to alternative sources of funds is outstanding, Safety is almost like risk free Government short-term obligations.
ST-2	High Grade High certainty of timely payment. Liquidity factors are strong and supported by good fundamental protection factors. Risk factors are very small.
ST-3	Good Grade Good certainty of timely payment. Liquidity factors and company fundamentals are sound. Although ongoing funding needs may enlarge total financing requirements, access to capital markets is good. Risk factors are small.
ST-4	Satisfactory Grade Satisfactory liquidity and other protection factors qualify issues as to investment grade. Risk factors are larger and subject to more variation.
ST-5	Non-Investment Grade Speculative investment characteristics. Liquidity is not sufficient to insure against disruption in debt service. Operating factors and market access may be subject to a high degree of variation.
ST-6	Default Issuer failed to meet scheduled principal and/or interest payments.