



## The Pakistan Credit Rating Agency Limited

### Rating Report

#### Spectrum Securities Limited | BFR

##### Report Contents

1. Rating Analysis
2. Financial Information
3. Rating Scale
4. Regulatory and Supplementary Disclosure

##### Rating History

Dissemination Date	Rating	Outlook	Action	Rating Watch
20-Dec-2021	BFR 3	Stable	Initial	-

#### Rating Rationale

Factor	Comment
<b>Ownership</b>	Controlling stakes are held by Mr. Muhammad Owais at ~51%. The CEO Mr. Ahmed Nabeel also owns ~20% of the ownership.
<b>Governance</b>	The Company's board comprise of three directors including the CEO while the presence of independent director is well noted.
<b>Management and Client Services</b>	SSL has an adequately defined organizational structure. Clients have access to research portal, while grievance procedures are also in place.
<b>Internal Controls and Regulatory Compliance</b>	The internal audit and compliance functions are segregated; however, the audit committee lacks independence.
<b>Business Sustainability</b>	Ratings are constrained by the Company's significant dependence on equity brokerage operations, limited diversification of income streams.
<b>Financial Sustainability</b>	The Company has an adequate capitalization level, Net Capital Balance stands at ~PKR 92mln at end-Jun'21.

#### Key Rating Drivers

The assigned rating of Spectrum Securities Limited ("SSL" or the "Company") incorporates adequate ownership structure and governance framework. Increasing the board size and inclusion of independent director in board level committees may result in improved governance framework. SSL's services mainly comprise of equity brokerage where it has a good mix of corporate/institutional and HNWI's. SSL has adequately defined organizational hierarchy where the responsibilities and reporting lines are structured. SSL provides prudent services to its clients with access to technical and fundamental reports and a dynamic reporting mechanism. Client services may be further enhanced through complaint tracking system. SSL has a sound IT infrastructure supported by established IT policy. Contingency measures are in place with off-site data backup. The internal control and regulatory compliance is considered sound whereby the Company has established Trading Policy and Procedures to deal with any potential conflict with clients trades. Segregation of Head of Finance and Compliance may strengthen the compliance function. The rating incorporates low leveraged capital structure of the Company. Timely materialization of outstanding receivables is important. At end-Jun'21, the brokerage revenue clocked in at ~PKR 118mln (SPLY: ~PKR 55mln) and the equity improved to ~PKR 187mln at end-Jun'21 (SPLY: ~PKR 135mln). Improvement in equity through further capital injection and reduction in outstanding receivables will be important, going forward.

##### Disclosure

<b>Name of Rated Entity</b>	Spectrum Securities Limited   BFR
<b>Type of Relationship</b>	Solicited
<b>Purpose of the Rating</b>	Broker Fiduciary Rating (BFR)
<b>Applicable Criteria</b>	Methodology   Broker Fiduciary Rating(Jan-21)
<b>Related Research</b>	Sector Study   Brokerage & Securities(Jan-21)
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## Profile

**Background:** Spectrum Securities Limited, “SSL or The Company” was incorporated under the Companies Ordinance 1984 in 2014 after the acquisition of TREC from M/S Mazhar Hussain Securities (Pvt.) Limited in the year 2000. SSL is a Corporate Member of the Pakistan Stock Exchange and registered with the SECP.

**Operations:** SSL’s service offering includes Economic and Investment Research and Equity Brokerage. The clientele of the Company is segmented into three categories i) HNWI ii) financial institutions/corporates iii) retail.

## Ownership

**Ownership Structure:** SSL is primarily owned by individuals. Controlling stakes are held by Mr. Muhammad Owais at ~51%, while the CEO Mr. Ahmed Nabeel also owns ~20% of the ownership.

**Stability:** Formation of written shareholding agreement and succession plan would be a strengthening factor.

**Business Acumen:** The Company’s sponsor possesses relevant educational background and extensive industry specific working knowledge. The overall assessment of strategic thinking capability of sponsors is comfortable.

**Financial Strength:** The sponsors have sizeable net worth and may inject capital in the Company with increasing quantum of operations. This also shows the sponsors commitment in case financial need arises.

## Governance

**Board Structure:** The Company’s board comprise of three directors including the CEO – Mr. Ahmed Nabeel. Mr. Muhammad Imran Arif (COO) serves as an executive director while Mr. Munir Hussain is an independent director which enhances the governance profile.

**Members’ Profile:** The board possess the necessary skills and experience required for capital markets. The board members, on-average, possess more than ~20 years of experience in the field of finance and capital markets.

**Board Effectiveness:** To ensure an effective control environment and compliance with reporting standards, the Company has constituted an Audit Committee, HR Committee, Risk Management Committee and Investment Decision Making Committee. The Audit Committee conducts meetings at minimum of once every quarter and the internal auditor reports are presented along with the findings.

**Transparency:** Nasir Javed Maqsood Imran & Co. has been engaged as the Company’s external auditors during FY21. The auditors are ranked as Category B auditor on the panel of SBP auditors list.

## Management and Client Services

**Organizational Structure:** The Company has an adequate organizational structure with an experienced management team and a balanced mix of professionals from the finance industry. The functions of the Company are mainly divided into 1) Sales, 2) Research, 3) Operations (Settlement, CS & IT), 4) HR, 5) Compliance and 6) Internal Audit.

**Management Team:** The CEO Mr. Ahmed Nabeel, the CFO Mr. Muhammad Umair Arif and the COO Mr. Muhammad Imran Arif act as part of the senior management of Spectrum Securities Limited. Mr. Ahmed Nabeel has an extensive and diversified experience in the field of capital market spanning over twenty-five years. Mr. Muhammad Umair possess Masters’s education and has been with the company since 2016 and serves as the CFO and Company Secretary. The Compliance department is also headed by Mr. Umair Arif.

**Client Servicing:** The Company has provided its customers with various channels, including a mobile app and online trading platform to facilitate them for execution and monitoring of their transactions.

**Complaint Management:** The Company has an adequate complaint management system supported by adequately defined policy. Complaints can be made via email, calls and website. The Company has also provided direct links to the regulators on its website.

## Internal Controls and Regulatory Compliance

**Extent of Automation / Integration:** The Company has integrated database platforms and can generate real time MIS reports on timely basis.

**Continuity of Operations:** The Company has well defined disaster recovery and Business Continuity plans supported by adequately drafted policies. The DRP/BCP systems are tested bi-annually with the secondary data storage site at different premises.

**Risk Management Framework:** To ensure operational efficiency and appraisal of internal controls, the Company has an in-house internal audit department, which implements and monitors the policies and procedures of the Company. Audit Committee is also responsible for overseeing the company's significant risk areas assessed by Management, Internal or external auditor as well as the related controls to mitigate such risk. An independent risk management department would have further strengthened the Risk Management Framework.

**Regulatory Compliance:** Compliance Department ensures regular monitoring of controls and systems, which ensures all functions are in-line with the applicable policies and procedures. Research analyst policy has also been formulated. However, separation of Compliance and Finance function is encouraged.

## Business Sustainability

**Operating Environment:** Despite of attractive market fundamentals, during CY21 through October, the stock market has delivered a modest 5.6% return. The prevailing market valuations reflect overblown pessimism and positive view on the stock market are driven by: (i) attractive valuations, (ii) robust corporate profitability, (iii) abundant market liquidity, and (iv) easier financial conditions. The successful completion of the review will pave the way for the release of the USD 1bln from the IMF and facilitate flows from other multilateral agencies such as the Asian Development Bank, World Bank, and Islamic Development Bank.

**Performance:** The Company's main source of revenue is from commission on equity brokerage which clocked in at ~PKR 118mln for FY21 (SPLY: ~PKR 55mln) on account of increased volumes in the market. Accordingly, the Company earned a net profit amounting ~PKR 39mln for FY21 (SPLY: ~PKR 9.6mln).

**Strategy:** The management has plans to capture the north markets. The long-term focus is to cater the institutional and HNW clientele.

## Financial Sustainability

**Credit Risk:** The Company has detailed KYC/CDD procedures in place for the assessment of the client's creditworthiness. However, the Company has outstanding receivables of ~PKR 76mln at end-Jun'21, timely materialization of which is important.

**Market Risk:** The Company is running its own proprietary book with market value of ~PKR 15mln at end-Jun'21. Since the magnitude of short-term investments at ~8% are nominal as compared to equity, the exposure to market risk remains low.

**Liquidity Risk:** The Company reported current assets of ~PKR 291mln for FY21 as compared to current liabilities of ~PKR 134mln. Liquid assets are considered adequate to account for current liabilities of the Company.

**Capitalization:** The Company has an adequate capitalization level with regulatory Net Capital Balance (NCB) standing at ~PKR 92mln at end-Jun'21. The Company's equity stood at ~PKR 187mln at end-Jun'21.

## Spectrum Securities Limited

Jun-21

Jun-20

Jun-19

12M

12M

12M

## A BALANCE SHEET

1 Finances	16	3	14
2 Investments	56	38	40
3 Other Earning Assets	146	81	42
4 Non-Earning Assets	103	80	55
5 Non-Performing Finances-net	-	-	-
<b>Total Assets</b>	321	202	152
6 Funding	10	10	-
7 Other Liabilities (Non-Interest Bearing)	124	57	24
<b>Total Liabilities</b>	134	67	24
<b>Equity</b>	187	135	127

## B INCOME STATEMENT

1 Fee Based Income	118	55	28
2 Operating Expenses	(100)	(50)	(40)
3 Non Fee Based Income	30	7	(7)
<b>Total Operating Income/(Loss)</b>	48	12	(20)
4 Financial Charges	(0)	(0)	(0)
<b>Pre-Tax Profit</b>	48	12	(20)
5 Taxes	(9)	(2)	(1)
<b>Profit After Tax</b>	39	10	(21)

## C RATIO ANALYSIS

## 1 Business Sustainability

Pre Tax Margin	40.6%	21.3%	-70.2%
EBITDA/ Revenue	42.0%	23.2%	-65.8%
Profit / (Loss) Before Interest & Taxes / Total Assets	14.9%	5.7%	-12.9%

## 2 Financial Sustainability

Total Investments / Equity	30.1%	28.0%	31.3%
NCB / Equity	49.1%	54.7%	63.1%
LCB/ Total Equity	49.7%	46.4%	49.4%
( Cash & Cash Equivalents + Government Securities ) / Total Assets	74.2%	74.5%	58.2%
Total Debt / Equity	5.3%	7.4%	0.0%

## Broker Fiduciary Rating Scale & Definitions

An independent opinion on the quality of management, client services and sustainability of operations

Scale	Definition
<b>BFR 1</b>	<b>Very Strong.</b> Very strong quality of management, client services and very high likelihood of sustaining operations
<b>BFR 2++</b> <b>BFR 2+</b> <b>BFR 2</b>	<b>Strong.</b> Strong quality of management, client services and high likelihood of sustaining operations
<b>BFR 3++</b> <b>BFR 3+</b> <b>BFR 3</b>	<b>Good.</b> Good quality of management, client services and above average likelihood of sustaining operations
<b>BFR 4++</b> <b>BFR 4+</b> <b>BFR 4</b>	<b>Adequate.</b> Adequate quality of management, client services and average likelihood of sustaining operations
<b>BFR 5</b>	<b>Weak.</b> Weak quality of management, client services weak likelihood of sustaining operations

**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 some material identifiable event with indeterminable rating implications. 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 rating 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 rating remains suspended for six months, or/and d) PACRA finds it impractical to surveill the opinion due to lack of requisite information.

**Harmonization** A change in rating due to revision in applicable methodology or underlying scale.

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(1) Rating is just an opinion about the creditworthiness of the entity and does not constitute recommendation to buy, hold or sell any security of the entity rated or to buy, hold or sell the security rated, as the case may be | Chapter III; 14-3-(x)

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- i. The Rating Team or any of their family members have no interest in this rating | Chapter III; 12-2-(j)
- ii. PACRA, the analysts involved in the rating process and members of its rating committee, and their family members, do not have any conflict of interest relating to the rating done by them | Chapter III; 12-2-(e) & (k)
- iii. The analyst is not a substantial shareholder of the customer being rated by PACRA [Annexure F; d-(ii)] Explanation: for the purpose of above clause, the term "family members" shall include only those family members who are dependent on the analyst and members of the rating committee

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- (4) PACRA does not disclose or discuss with outside parties or make improper use of the non-public information which has come to its knowledge during business relationship with the customer | Chapter III; 10-7-(d)
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- (7) PACRA uses due care in preparation of this Rating Report. Our information has been obtained from sources we consider to be reliable but its accuracy or completeness is not guaranteed. PACRA does not, in every instance, independently verifies or validates information received in the rating process or in preparing this Rating Report.
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- (9) PACRA ensures before commencement of the rating process that an analyst or employee has not had a recent employment or other significant business or personal relationship with the rated entity that may cause or may be perceived as causing a conflict of interest; | Chapter III; 11-A-(r)
- (10) PACRA maintains principal of integrity in seeking rating business | Chapter III; 11-A-(u)
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- (12) PACRA receives compensation from the entity being rated or any third party for the rating services it offers. The receipt of this compensation has no influence on PACRA's opinions or other analytical processes. In all instances, PACRA is committed to preserving the objectivity, integrity and independence of its ratings. Our relationship is governed by two distinct mandates i) rating mandate - signed with the entity being rated or issuer of the debt instrument, and fee mandate - signed with the payer, which can be different from the entity
- (13) PACRA does not provide consultancy/advisory services or other services to any of its customers or to any of its customers' associated companies and associated undertakings that is being rated or has been rated by it during the preceding three years unless it has adequate mechanism in place ensuring that provision of such services does not lead to a conflict of interest situation with its rating activities; | Chapter III; 12-2-(d)
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- (15) PACRA ensures that the rating assigned to an entity or instrument is not be affected by the existence of a business relationship between PACRA and the entity or any other party, or the non-existence of such a relationship | Chapter III; 12-2-(i)
- (16) PACRA ensures that the analysts or any of their family members shall not buy or sell or engage in any transaction in any security which falls in the analyst's area of primary analytical responsibility. This clause shall, however, not be applicable on investment in securities through collective investment schemes. | Chapter III; 12-2-(l)
- (17) PACRA has established policies and procedure governing investments and trading in securities by its employees and for monitoring the same to prevent insider trading, market manipulation or any other market abuse | Chapter III; 11-B-(g)

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- (18) PACRA monitors all the outstanding ratings continuously and any potential change therein due to any event associated with the issuer, the security arrangement, the industry etc., is disseminated to the market, immediately and in effective manner, after appropriate consultation with the entity/issuer; | Chapter III | 18-(a)
- (19) PACRA reviews all the outstanding ratings on semi-annual basis or as and when required by any creditor or upon the occurrence of such an event which requires to do so; | Chapter III | 18-(b)
- (20) PACRA initiates immediate review of the outstanding rating upon becoming aware of any information that may reasonably be expected to result in downgrading of the rating; | Chapter III | 18-(c)
- (21) PACRA engages with the issuer and the debt securities trustee, to remain updated on all information pertaining to the rating of the entity/instrument; | Chapter III | 18-(d)

### **Probability of Default**

(22) PACRA's Rating Scale reflects the expectation of credit risk. The highest rating has the lowest relative likelihood of default (i.e, probability). PACRA's transition studies capture the historical performance behavior of a specific rating notch. Transition behavior of the assigned rating can be obtained from PACRA's Transition Study available at our website. (www.pacra.com). However, actual transition of rating may not follow the pattern observed in the past | Chapter III | 14-(f-VII)

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