



The Pakistan Credit Rating Agency Limited

BROKER MANAGEMENT RATING

ARIF HABIB LIMITED

| BROKERAGE HOUSE | RATING (INITIAL) | DATE | DEFINITION | RATING SCALE | |
|--|------------------|-----------|--|--------------|------------|
| Arif Habib Limited (AHL) | BMR1 | 16-Jan-18 | Aims to facilitate users to differentiate between brokers on the basis of quality of management and services provided. | BMR1A | Excellent |
| | | | | BMR1 | Strong |
| | | | | BMR2 | Sound |
| | | | | BMR3 | Adequate |
| | | | | BMR4 | Inadequate |
| | | | | BMR5 | Weak |
| <small>(+) or (++) may be appended to a rating except BMR 1A and BMR 5</small> | | | | | |

RATING RATIONALE

Broker Management Rating of Arif Habib Limited captures its leading position in the country's brokerage industry emanating from established franchise, deep relationship with diverse customer base, and strong system share. This is underpinned by its well-developed transactions execution and monitoring system, acclaimed research, strong control environment, and good governance framework. It offers various value added services to its clients including online trading terminal, research portal and mobile app. Strong IT infrastructure emplaced under proper guidance of IT steering committee to ensure uniform efficiency.

In addition to brokerage, AHL enjoys distinct position in investment banking and advisory domain. This provides deeper penetration into client base. Credit risk – customer's receivables and funding – remains low. AHL has high exposure to market risk. It maintains sizeable strategic and trading book. Related risks are managed through well-defined investment policy. Liquidity risk is supported by firm commitment from sponsor for strategic book. AHL enjoys robust profitability.

The rating requires upholding strong control and governance framework, continuing update of client servicing tools, and careful monitoring of risks - mainly liquidity and conflict of interest - emanating from investment activities.

Report Contents

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| ARIF HABIB LIMITED | |
|-----------------------------|---|
| Incorporated | 2004 |
| Major business lines | <ul style="list-style-type: none"> ▪ Brokerage – shares, money market, forex, commodity ▪ Investment banking and advisory ▪ Securities research ▪ Equities investments ▪ Financing |
| Legal status | Public Limited |

| INDUSTRY SNAPSHOT |
|--|
| <ul style="list-style-type: none"> ▪ Fragmented industry with 305 brokers (SECP list of registered brokers as on Nov 30, 2016). ▪ Total number of registered UINs as on June 30, 2017 – 245,758. ▪ Total number of listed scrips - 529 as on June 30, 2017. ▪ Stringent regulatory framework governed by SECP, PSX, NCCPL and CDC. |

| | |
|-----------------------------------|---------------|
| OWNERSHIP & GOVERNANCE | STRONG |
|-----------------------------------|---------------|

- **Profile** – AHL is a part of Arif Habib group. Company’s major shareholder is Arif Habib Corporation, holding 65.52% of AHL. Ultimate owner of the group is Mr. Arif Habib, an established entrepreneur. Operating in multiple sectors, the group has presence in fertilizer, power, cement, real estate and financial segment.
- **Board** – The Company has a well composed board. It has seven members including CEO Mr. Muhammad Shahid Ali. Two members are independent and four are non-executive. Board quarterly review overall performance of the company.
- **Audit & Sub Committees** – Audit committee is chaired by Mr. Ali Murtaza kazmi, an independent director, ensuring good corporate governance practice. The committee meets every quarter to analyze financial statistics and review internal audit report. AHL is maintaining IT steering and HR committees. These provide assistance and expert guidance.

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| MANAGEMENT QUALITY | STRONG |
|---------------------------|---------------|

- **Key Personnel** – AHL top management is well qualified and experienced. Mr. Muhammad Shahid Ali (CEO) has 20 years of professional experience.
- **Organization Structure** – Clear departmentalization provides efficient use of resources. AHL follows the best practices of the industry; departments are clearly defined and headed by seasoned professionals.
- **Sales & Trading Staff** – Lately, Mr. Saad Bin Ahmed joined AHL as a head of sales; he has over 17 years of professional experience. Low employee turnover and well defined induction and training process ensures the effectiveness of sales team.

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| CUSTOMER RELATIONSHIP | SOUND |
|------------------------------|--------------|

- **Client Servicing** – Offers multiple account opening mediums. Similarly multiple channels are available to customers to execute and monitor their transactions. All of the information is easily available at company’s website to ease customer reach.
- **Reporting** – AHL has strong client reporting mechanism with various market reports being sent to clients on daily basis to keep them update.
- **Trading Facilities** – Modern online trading facility along with upright online trading terminal having updated trading tools and features. AHL provides also mobile app for trading and information.
- **Complaints Management** – Adequate complaint management system in place, complaints can be made via e-mail, SMS and calls. AHL has centralized complaint logging and follow up tools available.

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| IT INFRASTRUCTURE ADEQUACY | STRONG |
|-----------------------------------|---------------|

- **Integration** – Two database platforms installed with full integration between back and front office, have ability to generate real time reports.
- **Network Stability** – Company has established efficient backup line that instantly revert the connection to alternate gateway in an automated fashion.
- **Operational Continuity** – AHL has detailed disaster recovery plan to ensure the business continuity at the time of disaster. Moreover backups are maintained at DR site.

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| RISK MANAGEMENT | SOUND |
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- **Operational Risk** – Management has adopted rigorous policies and procedures to identify and monitor risks at operational level. Existence of confidentiality barriers improves the risk profile.
- **Credit Risk** – For proper assessment of customer creditworthiness, AHL emplaced KYC along with client due diligence policies. Applicable MF and MTS policies adopted and funding limits are fully defined.
- **Market Risk** – Company is maintaining a proprietary book for investment in different asset classes and all of the investments are properly managed and monitored according to AHL’s investment policy. Proper dedicated team assigned (including CEO) to manage the investments. Cut-off limits are fully defined. Additionally, AHL has firm commitment from its Sponsor to buy back strategic investment from short term portfolio at time of liquidity needs. In any case, the investment book has risk of conflict of interest, though being managed carefully.

REGULATORY COMPLIANCE**SOUND**

- **Internal Audit & Compliance** – AHL has in house internal audit department. It is effective and properly report its observations. Company has effective compliance department which regularly monitors the system and controls to ensure that all functions are doing in line with the applicable policies and procedures.
- **System Audit & Regulatory Filing** – No observation found during the system audit. No matters were raised by the regulators during the last year.

BUSINESS AND FINANCIAL STABILITY**STRONG**

- **Business Risk** – Prominent player in equity broking, having strong alliance with leading foreign broker/dealers. AHL's market share is growing (currently ~ 9%). However, company's branch network is less compared to other major players. It has a good mix of foreign, local institutional and high net worth individual clients. Retail penetration needs attention. AHL has distinctive edge over others with its strong foot hold in investment banking and advisory business. This segment matches broking revenue and is growing. Investment book yields a substantial source of revenue, though volatile. Overall, AHL yields strong profitability. This cushions against volatile behavior of investment book.
- **Financial Risk** – AHL's Net Capital balance (NCB) stood at PKR 1,775mln on 30th June 17. The company avails financing to fund its core working capital needs mainly. Sometimes, these are utilized for its financing and investment operations.



| BALANCE SHEET | 30-Sep-17 <i>Un-Audited</i> | 30-Jun-17 <i>Audited</i> | 30-Jun-16 <i>Audited</i> | 30-Jun-15 <i>Audited</i> |
|---|--------------------------------|-----------------------------|-----------------------------|-----------------------------|
| EARNING ASSETS | | | | |
| 1 Finances | 563 | 559 | 36 | - |
| 2 Investments | 5,433 | 4,522 | 4,319 | 2,638 |
| | 5,996 | 5,082 | 4,355 | 2,638 |
| NON-EARNING ASSETS | | | | |
| 3 Cash and Bank Balances | 80 | 116 | 23 | 79 |
| 4 Trade debts | 74 | 75 | 582 | 537 |
| 5 Advances, Deposits and Other receivables | 224 | 370 | 541 | 714 |
| 6 Others (including Fixed Assets) | 50 | 51 | 62 | 66 |
| TOTAL ASSETS | 6,423 | 5,693 | 5,563 | 4,035 |
| 7 Equity | 2,685 | 3,201 | 2,706 | 2,681 |
| 8 Borrowings | 2,056 | 1,408 | 1,883 | 575 |
| Other Liabilities (Non-Interest Bearing) | | | | |
| 9 Trade Creditors | 1,487 | 904 | 872 | 570 |
| 10 Other Liabilities | 195 | 179 | 103 | 209 |
| TOTAL EQUITY & LIABILITIES | 6,423 | 5,693 | 5,563 | 4,035 |
| INCOME STATEMENT | 30-Sep-17 <i>Un-Audited</i> | 30-Jun-17 <i>Audited</i> | 30-Jun-16 <i>Audited</i> | 30-Jun-15 <i>Audited</i> |
| Fee Based Revenue | | | | |
| 11 Fees | 60 | 365 | 252 | 256 |
| 12 Brokerage | 66 | 402 | 277 | 323 |
| Operating Expenses | | | | |
| 13 Personnel Expenses | (53) | (207) | (159) | (185) |
| 14 Administrative Expenses | (20) | (79) | (106) | (151) |
| Fee Based Income / (Loss) | 53 | 481 | 264 | 243 |
| Non Fee-Based Income | | | | |
| 15 Bank Deposits and others | - | 28 | 25 | 10 |
| 16 Gain on Sale of Investments | (38) | 895 | (0) | 1,148 |
| 17 Others | 70 | (125) | 333 | (23) |
| Total Operating Income / (Loss) | 85 | 1,279 | 622 | 1,379 |
| 18 Financial Charges | (40) | (138) | (166) | (234) |
| Profit / (Loss) Before Tax | 45 | 1,141 | 456 | 1,145 |
| 19 Taxes | (12) | (260) | (47) | (217) |
| Net Income | 33 | 880 | 409 | 928 |
| RATIO ANALYSIS | 30-Sep-17 <i>Un-Audited</i> | 30-Jun-17 <i>Audited</i> | 30-Jun-16 <i>Audited</i> | 30-Jun-15 <i>Audited</i> |
| CREDIT RISK | | | | |
| 20 Accounts Receivable / Avg. Daily Value Traded | 4.8% | 4.2% | 52.9% | 58.9% |
| 21 Overdue (> 14 days) Accounts Receivable / Total Accounts Receivable | 34.5% | 36.8% | 11.9% | 10.0% |
| 22 Accounts Receivable / (Short Term Borrowings + Customer Advances + Accounts Payable) | 2.1% | 3.2% | 21.1% | 47.0% |
| LIQUIDITY RISK | | | | |
| 23 Trade Receivables / Trade Payables | 0.05 | 0.08 | 0.67 | 0.94 |
| 24 Liquid Assets / Trade Related Liabilities | 2.86 | 4.43 | 4.17 | 3.37 |
| 25 Liquid Assets / (Short term Borrowings + Advances from Customers + Accounts Payable) | 1.20 | 1.73 | 1.32 | 1.68 |
| BUSINESS RISK | | | | |
| 26 Net Profit (before tax) Margin | 35.8% | 148.6% | 86.2% | 197.6% |
| 27 Fee Based Income to Total Income | 80.0% | 49.0% | 59.7% | 33.8% |
| 28 Operating Cost-to-Total Income | 46.2% | 18.3% | 29.9% | 19.6% |
| 29 Net Fee based Income to Net Profit before Tax | 118.0% | 42.2% | 58.0% | 21.2% |
| 30 Net Profit (before tax) to Total Income | 28.6% | 72.9% | 51.4% | 66.8% |
| 31 Net Non-Earning Assets / Equity | 8.6% | 13.5% | 40.9% | 44.3% |
| FINANCIAL RISK | | | | |
| 32 Borrowings / Equity | 76.6% | 44.0% | 69.6% | 21.5% |
| 33 NCB / Equity | 53.2% | 55.5% | 35.2% | 47.4% |

BROKER MANAGEMENT RATING SCALE

| SYMBOL | DEFINITION | |
|-------------------------------------|-------------------|--|
| BMR 1A | Excellent | Excellent regulatory compliance, control environment, and financial management; governance and risk management frameworks are extremely effective; HR, IT, and customer services are strongly proactive. |
| BMR 1++ BMR 1+ BMR 1 | Strong | Strong regulatory compliance, control environment, and financial management; governance and risk management frameworks are highly effective; HR, IT, and customer services are highly proactive. |
| BMR 2++ BMR 2+ BMR 2 | Sound | Sound regulatory compliance, control environment, and financial management; governance and risk management frameworks are effective; HR, IT, and customer services are proactive. |
| BMR 3++ BMR 3+ BMR 3 | Adequate | Adequate regulatory compliance, control environment, and financial management; governance and risk management frameworks are satisfactory; HR, IT, and customer services are adequate. |
| BMR 4++ BMR 4+ BMR 4 | Inadequate | Inadequate regulatory compliance, control environment, and financial management; governance and risk management frameworks need improvements; HR, IT, and customer services are insufficient. |
| BMR 5 | Weak | Weak regulatory compliance and business practices. |

SURVEILLANCE AND VALIDITY OF THE RATING

PACRA shall not keep the Broker Management Rating under constant surveillance. The rating will be reviewed at least once every six months. Any material happening during a period that may warrant a revision of rating will be incorporated in the following review.

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’.

WITHDRAWN

A rating is withdrawn on a) termination of rating mandate, or b) cessation of underlying entity.

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| | | | |
|-----------------------|---|---------------------------|---------------|
| Name of Rated Entity | Arif Habib Limited | | |
| Sector | Brokerage | | |
| Type of Relationship | Solicited | | |
| Purpose of the Rating | Brokerage Management Rating | | |
| Applicable Criteria | Broker Management Rating Methodology (Sep 2017) | | |
| Sector Study | Securities Brokers (Oct 2017) | | |
| Rating Analyst | Shahzaib Khalid | Shahzaib.khalid@pacra.com | 042-3586 9504 |

Regulatory and Supplementary Disclosure

Rating Team Statements

(1) Broker Management Rating is an opinion on the quality of management and services provided by the broker 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)**

(2) Conflict of Interest

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 Restrictions

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(5) PACRA does not make proposals or recommendations regarding the activities of rated entities that could impact a credit rating of entity subject to rating | **Chapter III; 10-7-(k)**

Conduct of Business

(6) PACRA fulfills its obligations in a fair, efficient, transparent and ethical manner and renders high standards of services in performing its functions and obligations; | **Chapter III; 11-A-(a)**

(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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(10) PACRA maintains principal of integrity in seeking rating business | **Chapter III; 11-A-(u)**

(11) PACRA promptly investigates, in the event of a misconduct or a breach of the policies, procedures and controls, and takes appropriate steps to rectify any weaknesses to prevent any recurrence along with suitable punitive action against the responsible employee(s) | **Chapter III; 11-B-(m)**

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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

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(14) PACRA discloses that no shareholder directly or indirectly holding 10% or more of the share capital of PACRA also holds directly or indirectly 10% or more of the share capital of the entity which is subject to rating or the entity which issued the instrument subject to rating by PACRA; | Reference **Chapter III; 12-2-(f)**

(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)**

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(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)**

Monitoring and review

(18) PACRA does not monitor BMR on continuous basis. Any potential change therein due to any event associated with the entity is incorporated in next review; | **Chapter III | 18-(a)**

(19) PACRA reviews all outstanding ratings on semi-annual basis | **Chapter III | 18-(b)**

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