



The Pakistan Credit Rating Agency Limited

Rating Report

Arif Habib Limited | BMR

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Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
18-Dec-2020	BMR1	-	Stable	Maintain	-
20-Dec-2019	BMR1	-	Stable	Maintain	-
20-Jun-2019	BMR1	-	Stable	Maintain	-
20-Dec-2018	BMR1	-	Stable	Maintain	-
16-Jan-2018	BMR1	-	Stable	Initial	-

Rating Rationale and Key Rating Drivers

The rating incorporates Arif Habib Limited's ("AHL" or "The Company") association with astute sponsors 'Arif Habib Group'. The leading position of the Company emanates from its stable market share, established branches, and strong operational control environment. AHL has well experienced management team, sound governance framework and well established compliance protocols which bodes well for the rating. In addition to brokerage, AHL achieved a distinct position in advisory domain in Pakistan, resulting in diversified revenue base and competitive advantage over peers. The Company has maintained a sizeable number of investors' accounts including Institutional, HNWI's and Retailers. AHL has established rigorous protocols regarding risk assessment by implementing KYC, CDD, AML, CFT and whistle blowing policies. On investor's front, investor's guidelines, multiple account opening mediums and complaint management policies and procedures are in place. The Company offers various value-added services to its clients including an online trading terminal, research portal, and mobile app. The Company has largely exposed to market risk due to its sizeable proprietary trading book. Related risks are deterred through well defined investment policies. During 1QFY21, the Company achieved ~12% market share (1QFY20: ~10%) in the recent bull-run of stock market and posted a five years high profits supplemented by brokerage income and capital gains. The Net Capital Balance of the company reached up to ~PKR 1.5bln with an equity base of ~PKR 3.7bln as at end Sep'20.

Going forward, AHL will continue to focus on growing its retail clientele and branch network, which remains a core pillar of its strategy. On corporate advisory and underwriting front, the Company is expecting revenues from the segment, to depict healthy growth in the ongoing year given present mandates in the pipeline and expected materialization of ongoing projects.

The rating is dependent on upholding strong control framework while effectively managing risks, particularly associated with proprietary investment book. Meanwhile, improving profitability from core income and maintaining market share is critical.

Disclosure

Name of Rated Entity	Arif Habib Limited BMR
Type of Relationship	Solicited
Purpose of the Rating	Broker Management Rating
Applicable Criteria	Methodology BMR(Jun-20)
Related Research	Sector Study Brokerage & Securities(Jan-20)
Rating Analysts	Madiha Sohail madiha.sohail@pacra.com +92-42-35869504



Ownership

Ownership Structure Arif Habib Limited ("AHL" or "The Company") is a public listed company established in 2004. Arif Habib Corporation Limited is the major shareholder of the Company, holding 69.44%, Mr. Arif Habib holds 5.44% while Banks, DFI's & mutual fund and others hold 3.76% and General Public hold 21.33%. Arif Habib Corporation Limited is the holding company of Arif Habib group.

Stability The Company continues to enjoy strong support from the sponsoring family. The market share of the Company during 1QFY21 stood at ~12% (SPY: ~10%).

Business Acumen Arif Habib Group has a diversified investment portfolio and has presence in fertilizer, power, cement, steel, real estate, and financial sectors. The sponsoring family has an established track record, demonstrating strong business acumen.

Financial Strength The net worth of Arif Habib Group clocked in at ~PKR 222bln, whereas net equity of Arif Habib Corporation Limited (Parent Company) stood at ~PKR: 28.13bln as at end Sep'20.

Governance

Board Structure The Company has a well-composed board. There are seven members, including the CEO Mr. Shahid Ali Habib. Two members are independent and four are non-executive. There is adequate female representation on board, in compliance with Code of Corporate Governance.

Members' Profile Mr. Zafar Alam is the current Chairman of the board. He is a master's degree holder in Nuclear Physics and possesses decades of experience in Investment Banking. Mr. Shahid Ali Habib completed his MBA from IBA Karachi and has a certification in Finance from London School of Economics (LSE). He carries over 21 years of experience in the fields of Securities Brokerage, Banking, Asset Management and Investment Banking.

Board Effectiveness To support board functions, the Company has established Audit and HR & remuneration committees. Both committees are chaired by Mr. Muhammad Sohail Salat, an independent director.

Transparency The Company has well established and independent internal audit function. Russell Bedford Rahman Sarfaraz Rahim Iqbal Rafiq (RSRIR) are the external auditors of the Company. The audit firm incorporated key matters paragraph in audit report regarding i) First time application of IFRS 9 ii) Valuation of investment property and iii) Valuation of unquoted investments in equity securities. The auditors issued an unqualified opinion on the financial statements for the period ending FY20.

Management

Management Team The Company has a team of seasoned professionals. Mr. Taha Siddiqui (CFO) is an ACCA member and has diversified experience in the fields of Financial, Manufacturing, Trading and Services industries. Mr. Saad Bin Ahmed (Head of Sales) possesses more than 17 years of international diversified experience in investment banking and financial services. The management staff turnover is low, indicating stability of the human resource.

Organizational Structure Arif Habib Limited has a functional organizational structure, with eight primary departments and six secondary departments. The primary departments include, i) International brokerage, ii) Domestic brokerage, iii) Inter-bank brokerage, iv) Investment Banking, v) Risk & Compliance, vi) Marketing & business development, vii) IT and viii) Online sales. Heads of the primary departments report directly to the CEO. Clear departmentalization offers efficient use of resources.

Client Servicing The Company offers multiple account opening mediums. Similarly, various channels, including a mobile app, are available to customers to execute and monitor their transactions. The Company has strong client reporting mechanism with account statements and market reports communicated to the clients on regular basis.

Complaint Management An adequate complaint management system is in place. Complaints can be made via e-mail, SMS, and calls.

Extent Of Automation / Integration Two database platforms are installed with full integration between back and front office. The system has the ability to generate timely reports. The system incorporates primary and secondary level protection.

Continuity Of Operations AHL has a detailed disaster recovery plan to ensure the business continuity at the time of disaster. Moreover, backups are maintained on daily basis.

Risk Management Framework The Board of Directors has overall responsibility for the establishment and oversight of Company's risk management framework. All treasury related transactions are carried out within the parameters of these policies.

Regulatory Compliance Risk Management & Compliance Department ensures regular monitoring of controls and systems, which ensures all functions are inline with the applicable policies and procedures. No observations were reported by the regulators during 1QFY21.

Business Sustainability

Business Risk As the COVID-19 pandemic triggered the deepest global recession in decades, The Pakistan Stock Market also remained under par with the world markets. The SBP responded to the unprecedented situation, by addressing monetary easing and debt moratorium. Whereas, certain proactive measures taken by SECP of trading halts, circuit limits, relaxation in Base Minimum Capital (BMC) requirements, and linking of short sell with uptick/zero plus rule, were geared to provide respite to the market participants. The Pakistan Stock Market now witnessing a rising trend, during 5MFY21, KSE-100 index touched the highest point of 42647 on 10th Sep'20, and currently stood at 41069 points posting a positive return of 19% since start of FY21. The traded volumes remained elevated over the 5MFY21, at an average of ~265mln (SPY: ~110mln), despite large market swings amidst COVID-19 implications. Going forward, the index is expected to recover with the COVID-19 vaccines expected to roll out in the coming months. Concern over pandemic is likely to reduce while improvement in economic activity is likely to accelerate globally as well as locally in medium term. Given the operating environment, players with efficient and variable cost structures focusing on high margin business and diversification in revenue streams are expected to fare better vis-à-vis peers. Furthermore, high traded volumes would bode well for brokerage firms.

Business Profile The Company possesses ~12% market share in equity brokerage, and has a strong relationship with leading foreign broker/dealers. AHL has a diversified revenue stream. The Company's branch network is expanding. It has a good mix of foreign, local institutional and high net worth individual clients. Retail side of the Company has also established and penetrated in the market. Historically, the Company had a distinct edge over its competitor's by having a strong foothold in investment banking and advisory business. However, in recent times the competition is catching up. One of the revenue streams of the Company pertains to proprietary investments, which make the Company largely exposed to market risk.

Revenue And Profitability Analysis The Company's topline posted ~118% increase and stood at ~PKR: 178mln (1QFY21: ~PKR 82mln). The core brokerage income of the Company witnessed an increase of 234%, clocked in at ~PKR 160mln (1QFY21: ~PKR 48mln) on the back of hefty traded volumes on PSX, meanwhile the administrative and operative expenses surged by 54% to ~PKR 104mln (1QFY21: ~PKR 68mln). The finance cost of the Company considerably shrank by ~53% to PKR 51mln (1QFY21: ~PKR 107mln) on the back of declined interest rates. The company posted net profits of ~PKR: 739mln (1QFY21: Net Loss ~PKR: 186mln). The profit can be attributable to capital gain on sale of investment (~PKR: 338mln) and unrealized loss on re-measurement of short term investment (~PKR: 337mln).

Financial Sustainability

Credit Risk The Company has developed enhanced due diligence procedures in addition to its KYC for the assessment of client creditworthiness. Applicable policies for leveraged products have been adopted and limits have been defined, which are strictly monitored.

Market Risk The Company maintains proprietary and investment book in different asset classes. All investments are properly managed and monitored according to the Company's investment policy. The proprietary investment to net equity ratio of the Company stood at ~64% (FY20: ~117%). A dedicated team (including CEO) manages the investments. Cut-off limits have been defined and are properly adhered to. Additionally, the Company has a firm commitment from its Sponsor to buy back strategic investment from short-term portfolio at a time of liquidity needs. The investment book has the risk of conflict of interest, though measures have been taken to mitigate it.

Liquidity Profile At end 1QFY21, liquid assets of the Company comprised ~0.34x of the total assets (FY19: ~0.5x). The Company has cumulative bank lines of ~PKR 4.7bln available in case a need arises. The utilized lines were ~PKR 3 bln, leaving ample room to borrow.

Financial Risk The Company's Net Capital Balance for 1QFY21 stood at ~PKR 1465mln (FY20: ~PKR 936mln). AHL finances its investments through short term debt and internally generated cash-flows.



PKR mln

Arif Habib Limited
Listed Public Limited

Sep-20	Jun-20	Mar-20	Dec-19	Sep-19	Jun-19	Jun-18
3M	12M	9M	6M	3M	12M	12M

A BALANCE SHEET

1 Finances	99	43	59	247	53	121	372
2 Investments	4,302	5,632	4,514	4,393	5,671	4,292	4,213
3 Other Earning Assets	921	777	801	1,176	454	596	662
4 Non-Earning Assets	826	440	516	392	701	634	321
5 Non-Performing Finances-net	-	-	-	-	-	-	-
Total Assets	6,148	6,893	5,890	6,208	6,880	5,642	5,567
6 Funding	2,220	3,484	2,531	3,022	4,219	2,578	2,151
7 Other Liabilities (Non-Interest Bearing)	267	142	931	176	161	147	135
Total Liabilities	2,487	3,626	3,462	3,199	4,380	2,725	2,286
Equity	3,661	3,266	2,428	3,010	2,500	2,918	3,187

B INCOME STATEMENT

1 Fee Based Income	178	505	356	215	82	679	547
2 Operating Expenses	(104)	(356)	(251)	(164)	(68)	(403)	(381)
3 Non Fee Based Income	734	343	56	521	(80)	(45)	672
Total Operating Income/(Loss)	808	491	161	573	(66)	231	838
4 Financial Charges	(51)	(362)	(300)	(226)	(107)	(218)	(185)
Pre-Tax Profit	757	129	(139)	346	(173)	12	653
5 Taxes	(19)	(69)	(29)	(23)	(13)	(75)	(117)
Profit After Tax	739	60	(169)	323	(186)	(62)	536

C RATIO ANALYSIS

1 Cost Structure

Financial Charges / Total Operating Income/(Loss)	6.3%	73.7%	186.7%	39.5%	-162.8%	94.7%	22.1%
Return on Equity (ROE)	389.3%	3.4%	-11.0%	77.0%	-0.7%	-2.0%	36.0%

2 Capital Adequacy

Equity / Total Assets (D+E+F)	59.5%	47.4%	41.2%	48.5%	36.3%	51.7%	57.3%
Free Cash Flows from Operations (FCFO) / (Financial Charges + Current M	51.4%	-34.4%	-61.4%	-68.8%	-33.7%	-58.6%	-73.5%

3 Liquidity

Liquid Assets / Total Assets (D+E+F)	43.6%	54.6%	40.8%	37.5%	56.4%	40.9%	25.4%
Liquid Assets / Trade Related Liabilities	278.9%	456.8%	292.7%	206.4%	306.9%	345.2%	208.3%

4 Credit & Market Risk

Accounts Receivable / Short-term Borrowings + Advances from Customers	8.2%	5.9%	3.6%	1.7%	1.0%	6.8%	1.1%
Equity Instruments / Investments	54.5%	64.3%	51.4%	52.5%	67.4%	50.2%	33.6%

Broker Management Rating

An independent opinion on the quality of management and services provided by the broker

Scale	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.

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 surveil the opinion due to lack of requisite information.

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

Surveillance. Surveillance on a publicly disseminated rating opinion is carried out on an ongoing basis till it is formally suspended or withdrawn. A comprehensive surveillance of rating opinion is carried out at least once every six months. However, a rating opinion may be reviewed in the intervening period if it is necessitated by any material happening.

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Rating Team Statements

(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)

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

- (3) No director, officer or employee of PACRA communicates the information, acquired by him for use for rating purposes, to any other person except where required under law to do so. | Chapter III; 10-(5)
- (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)
- (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.
- (8) PACRA prohibits its employees and analysts from soliciting money, gifts or favors from anyone with whom PACRA conducts business | Chapter III; 11-A-(q)
- (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)
- (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)

Independence & Conflict of interest

- (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)
- (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)
- (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)

Monitoring and review

- (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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