



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
30-Nov-2022	BFR 3	Stable	Maintain	-
20-Dec-2021	BFR 3	Stable	Initial	-

### Rating Rationale

Factor	Comment
<b>Ownership</b>	The majority stakes are controlled by Mr. Muhammad Owais who owns ~83% of the shares. The rating takes support from the sponsors business acumen. Mr. Owais is also engaged in the real estate business
<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 core income has declined leaving an impact on the Company's equity. The unrealized losses on proprietary book have further add up to the net loss.

### 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 takes comfort from a low leveraged capital structure. For FY22, the revenue from equity brokerage has declined YoY by ~42% which is in line with the drop in market volumes. Improvement in equity through internally generated profits is critical 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-22)
<b>Related Research</b>	Sector Study   Brokerage & Securities(Jan-22)
<b>Rating Analysts</b>	Afnan Iqbal   afnan.iqbal@pacra.com   +92-42-35869504

## Profile

**Background:** Spectrum Securities Limited, “SSL or the Company” was incorporated under the Companies Ordinance 1984 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 SECP.

**Operations:** SSL primarily provides the services of equity brokerage while clients are also facilitated with in-house research. The clientele of the Company is segregated into three categories i) HNWI ii) Financial institutions/Corporates iii) Retail.

## Ownership

**Ownership Structure:** The shareholding pattern has changed during the period under review. Mr. Muhammad Owais – who previously owned ~51% of the ownership rights now owns ~83% of the shares. The CEO, Mr. Ahmed Nabeel, and Mr. Asif Ibrahim divested their ownership during the year.

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

**Business Acumen:** The Company’s sponsor possesses relevant educational background and ample industry understanding. The overall assessment of strategic thinking proficiency of sponsors is comfortable.

**Financial Strength:** The sponsors have considerable 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 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 possesses 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 at board level.

**Transparency:** The financial statements of the Company for the period ended Jun-22 have been audited by Nasir Javed Masood Imran & Company Chartered Accountants – ranked in the category-B of the SBP. The auditors have issued an unqualified opinion on the financial statements for FY22.

## 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 SSL. Mr. Ahmed Nabeel has an extensive and diversified experience in the field of capital market spanning over twenty-five years. Mr. Muhammad Umair possesses Masters’ education and has been with the Company since 2015, where he 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 for execution and monitoring of their transactions. Moreover, SSL provides technical and fundamental research reports to its clients.

**Complaint Management:** The Company has an adequate complaint management system supported by adequately defined policy. Complaints can be made via email, calls and 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 a 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 responsible for overseeing the Company's significant risk areas; assessed by the management and internal or external auditor as well as the related controls to mitigate such risks. 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, the separation of compliance and finance functions is encouraged.

## Business Sustainability

**Operating Environment:** Pakistan's economy has been volatile so far during FY23, with the sustained high inflation and political instability getting further compounded by the devastating floods that have ravaged both the North and South of the country. The revival of the IMF program and receiving the tranche is a positive indication; however, the pressure on the domestic economy remains high due to implementation of further taxes and levies to continue to adhere to the IMF conditions. Going forward, the market may adopt a 'wait and see' approach for some time before volumes surge again as activity rebounds once the post-flood rebuilding starts.

**Performance:** The Company mainly earns revenue from commission on equity brokerage. According to the market volumes, the revenue has declined in FY22 as compared to FY21 as the institutional investors opted for fixed income asset class. SSL however turned its efforts towards retail segment and has added to the overall revenue. The core revenue for FY22 stands at ~PKR 68mln (SPLY: ~PKR 118mln) out of which ~PKR 55mln is earned from retail clients.

**Strategy:** The management intends to capture the north markets. The Company initially had its focus on institutional clients where it has a good reputation now. Going forward, the management intends to capture the retail market by opening up new branches.

## 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 21mln at end-Jun'22.

**Market Risk:** The Company is running its own proprietary book with market value of ~PKR 65mln which constitutes ~41% of the equity at end-Jun'22. This exposes the bottom line to market volatility.

**Liquidity Risk:** The Company reported current assets of ~PKR 206mln for FY22 as compared to current liabilities of ~PKR 84mln. Liquid assets are considered adequate to account for current liabilities of the Company.

**Capitalization:** The Company has an adequate capitalization level with Liquid Capital Balance (LCB) standing at ~PKR 49mln at end-Jun'22. The Company's equity stood at ~PKR 160mln at end- Jun'22. The equity has declined by ~PKR 27mln part of which could be attributable to the unrealized losses on proprietary book.

PKR mln

Spectrum Securities Limited	Jun-22	Jun-21	Jun-20
	12M	12M	12M

**A BALANCE SHEET**

1 Finances	21	16	3
2 Investments	82	56	38
3 Other Earning Assets	86	146	81
4 Non-Earning Assets	56	103	80
5 Non-Performing Finances-net	-	-	-
<b>Total Assets</b>	<b>244</b>	<b>321</b>	<b>202</b>
6 Funding	2	10	10
7 Other Liabilities (Non-Interest Bearing)	82	124	57
<b>Total Liabilities</b>	<b>84</b>	<b>134</b>	<b>67</b>
<b>Equity</b>	<b>160</b>	<b>187</b>	<b>135</b>

**B INCOME STATEMENT**

1 Fee Based Income	68	118	55
2 Operating Expenses	(89)	(100)	(50)
3 Non Fee Based Income	3	30	7
<b>Total Operating Income/(Loss)</b>	<b>(18)</b>	<b>48</b>	<b>12</b>
4 Financial Charges	(0)	(0)	(0)
<b>Pre-Tax Profit</b>	<b>(18)</b>	<b>48</b>	<b>12</b>
5 Taxes	(2)	(9)	(2)
<b>Profit After Tax</b>	<b>(20)</b>	<b>39</b>	<b>10</b>

**C RATIO ANALYSIS**

**1 Business Sustainability**

Pre Tax Margin	-26.2%	40.6%	21.3%
EBITDA/ Revenue	-23.3%	42.0%	23.2%
Profit / (Loss) Before Interest & Taxes / Total Assets	-7.3%	14.9%	5.7%

**2 Financial Sustainability**

Total Investments / Equity	51.4%	30.1%	28.0%
NCB / Equity	0.0%	0.0%	0.0%
LCB/ Total Equity	30.9%	49.8%	77.2%
( Cash & Cash Equivalents + Government Securities ) / Total Assets	50.2%	74.2%	74.5%
Total Debt / Equity	1.2%	5.3%	7.4%

### Broker Fiduciary Rating Scale & Definitions

An independent opinion on the quality of management and 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>BFR 5</b>	<b>Adequate.</b> Adequate quality of management, client services and average likelihood of sustaining operations.
	<b>Weak.</b> Weak quality of management, client services and weak likelihood of sustaining operations.

<p><b>Outlook (Stable, Positive, Negative, Developing)</b> 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'.</p>	<p><b>Rating Watch</b> 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.</p>	<p><b>Suspension</b> 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.</p>	<p><b>Withdrawn</b> 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.</p>	<p><b>Harmonization</b> A change in rating due to revision in applicable methodology or underlying scale.</p>
---	---	--	---	---

**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.

**Disclaimer:** PACRA has used due care in preparation of this document. Our information has been obtained from sources we consider to be reliable but its accuracy or completeness is not guaranteed. PACRA shall owe no liability whatsoever to any loss or damage caused by or resulting from any error in such information. Contents of PACRA documents may be used, with due care and in the right context, with credit to PACRA. Our reports and ratings constitute opinions, not recommendations to buy or to sell.

### **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 | Clause 11-(A)(p).
- (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)

### **Proprietary Information**

(23) All information contained herein is considered proprietary by PACRA. Hence, none of the information in this document can be copied or, otherwise reproduced, stored or disseminated in whole or in part in any form or by any means whatsoever by any person without PACRA's prior written consent