



The Pakistan Credit Rating Agency Limited

## Rating Report

### Arif Habib Limited | BFR

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#### Rating History

Dissemination Date	Rating	Outlook	Action	Rating Watch
17-Dec-2021	BFR 1	Stable	Maintain	-
29-Sep-2021	BFR 1	Stable	Initial	-

### Rating Rationale

Factor	Comment
<b>Ownership</b>	The Company is primarily corporate backed where ~69% stakes lies with Arif Habib Corporation Limited. Whereas, the general public hold 21% of the shares.
<b>Governance</b>	The Board comprises of seven directors including chairman and CEO. The Board complies with CCG Reg'2019 and posses manifold experience.
<b>Management and Client Services</b>	The Company has well-defined departmentalization headed by seasoned professionals. Well drafted policies are in place to ensure high quality of client service.
<b>Internal Controls and Regulatory Compliance</b>	The internal audit department, overseen by the audit committee, ensures compliance with the policies and procedures.
<b>Business Sustainability</b>	The revenue stream of the Company is well diversified among brokerage income, investment banking and others.
<b>Financial Sustainability</b>	The Company has strong capitalization indicators owing to the managed leveraging. However, the Company is exposed to market risk due to its proprietary investments.

### Key Rating Drivers

The assigned rating manifests the Company's association with astute sponsors 'Arif Habib Group', one of the prominent conglomerates in the country. The leading position of the Company emanates from its well-diversified revenue stream, stable market share, extensive outreach, and strong operational control environment. AHL has a 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 the advisory domain in Pakistan, resulting in a diversified revenue base and a competitive edge 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 whistleblowing policies. The Company has largely been exposed to market risk due to its sizeable proprietary trading book. Related risks are deterred through well-defined investment policies. During FY21, the Company posted its highest core profitability with net profits at ~PKR 2.1bln (FY20: ~PKR: 60mln), owing to record volumes achieved at PSX. The equity base of the Company amounted to ~PKR 4.9bln at end-FY21. Whereas, the Net Capital Balance of the Company reached up to ~PKR 1.9bln as at end-Jun'21.

#### Disclosure

<b>Name of Rated Entity</b>	Arif Habib 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)
<b>Rating Analysts</b>	Afnan Iqbal   afnan.iqbal@pacra.com   +92-42-35869504

## Profile

**Background:** Arif Habib Limited, “Arif Habib or the Company” is a licensed TREC holder of Pakistan Stock Exchange and was incorporated in 2004 under the Companies Act, 2017.

**Operations:** Arif Habib is a premier brokerage and financial services firm engaged in equity trading, investment banking, money market, forex trading, commodities trading, and securities research. The clientele of the Company is segmented into four categories i) HNWI’s ii) Financial Institutions iii) Retail iv) Foreign Broker Dealers.

## Ownership

**Ownership Structure:** Arif Habib Corporation Limited (AHCL) is the major shareholder of Arif Habib with ~69% equity stake. Mr. Arif Habib hold ~3% stake. Whereas, the general public hold ~21% of the shares.

**Stability:** The Arif Habib Group (AHG) ranks amongst the fastest growing multi-sector group in Pakistan. It has strong ability in identifying and developing successful enterprises.

**Business Acumen:** AHG holds interest in securities brokerage, investment and financial advisory, private equity, investment management, fertilizer, cement, steel, real estate, and energy sectors. Mr. Arif Habib holds vast experience in diverse sectors. Under his leadership, AHCL won several prestigious national and regional awards in recognition of its remarkable financial performance and sound corporate governance practices.

**Financial Strength:** The un-consolidated profit after tax of the Arif Habib Corporation Limited stood at ~PKR 3,874mln for FY21 while the equity also increased from ~PKR 18bln in FY20 to ~PKR 21bln in FY21.

## Governance

**Board Structure:** The Company has seven directors on the board including CEO and Chairman. There are four non-executive directors and two independent directors. The presence of independent directors strengthens the Company’s profile from the rating perspective.

**Members’ Profile:** Mr. Zafar Alam, the chairman has over 31 years of experience in investment banking. Overall, the board possesses the necessary skills and experience required for capital markets.

**Board Effectiveness:** There are three board committees in place – (i) Audit Committee (ii) Risk & Compliance Committee (iii) HR & Remuneration Committee. The board held four meetings during the period, which were attended by the majority of the members.

**Transparency:** The external auditors of the Company are Rahman Sarfaraz Rahim Iqbal Rafiq, they have expressed an unqualified opinion on the financial statements for FY21. The firm is in the A Category of SBP’s panel of auditors.

## Management and Client Services

**Organizational Structure:** Arif Habib has a multi-tier functional organization structure, consisting of the following departments, i) Finance, ii) Risk management & compliance, iii) IT, iv) Equity operations, v) Research, vi) International sales, vii) Online trading, and, viii) Commodity trading. Heads of the above-listed departments report directly to the CEO. There is an independent Internal Audit Department reportable to Audit Committee.

**Management Team:** The Company has a team of seasoned professionals headed by Mr. Shahid Ali Habib, the CEO. Mr. Shahid Ali Habib brings across over 23 years of experience in the fields of Securities Brokerage, Banking, Asset Management, and Investment Banking. Mr. Taha Siddiqui (CFO) is an ACCA member and has diversified experience in the fields of Financial, Manufacturing, Trading, and Services industries. The management staff turnover is low, indicating the stability of the human resource.

**Client Servicing:** The Company offers multiple accounts opening mediums. Similarly, various channels, including a mobile app, are available to customers to execute and monitor their transactions.

**Complaint Management:** An adequate complaint management system is in place. Complaints can be made via e-mail, SMS, and calls. Direct links for PSX and SECP are also available on the website to lodge complaints.

## Internal Controls and Regulatory Compliance

**Extent of Automation / Integration:** Two database platforms are installed with full integration between the back and front office.

**Continuity of Operations:** Arif Habib has a detailed disaster recovery plan to ensure 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 the Company's risk management framework. The audit committee is responsible for overseeing the Company's significant risk areas assessed by Management, Internal or external auditors as well as the related controls to mitigate such risk.

**Regulatory Compliance:** Risk Management & Compliance Department ensures regular monitoring of controls and systems, which ensures all functions are in line with the applicable policies and procedures.

## Business Sustainability

**Operating Environment:** PSX staged a phenomenal recovery in FY21 as the KSE-100 Index rose by 37% during the period. The growth came at the back of swift monetary and fiscal policy response, the success of the micro-lockdown strategy, robust remittances growth, and leverage reforms. Average traded volume attained the highest ever level at 528mln shares in FY21 (up by 169% from 196mln shares in FY20). Going forward, the delta variant poses a threat to the rising trend; however, the index is expected to recover as the COVID-19 vaccination reach record levels. Concern over pandemic is likely to reduce while improvement in economic activity is likely to accelerate globally as well as locally in the medium term.

**Performance:** The Company posted net profits of ~PKR: 2.08bln in FY21 (FY20: ~PKR: 60mln). The profit can be attributable to the significant increase in operating revenue by ~119% (SPLY: ~PKR 691mln) on the back of hefty trade volumes on PSX. While capital gain on the sale of investments and unrealized gain on short-term investment also contributed towards profitability. The advisory and consultancy stream of the Company experienced a momentous year as the revenue increased by ~3.3 times. The Company enlisted 6 out of the eight IPOs in CY21.

**Strategy:** The Company aims to build on its market leader status in the advisory domain and diversify its revenue streams. Further, the Company plans to promote retail investment with the help of digital initiatives.

## 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 books 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 ~55% (FY20: ~114%). A dedicated team (including CEO) manages the investments. Additionally, the Company has a firm commitment from its Sponsor to buy back strategic investment from the 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 Risk:** At end-FY21, liquid assets of the Company comprised ~0.32x of the total assets, (FY20: ~0.12x). The Company has cumulative bank lines of ~PKR 5.5bln available in case a need arises. The utilized lines were ~PKR 4.2bln, leaving ample room to borrow.

**Capitalization:** The Company's Net Capital Balance for end-Jun'21 stood at ~PKR 1.9bln (Jun'20: ~PKR 935mln). Arif Habib finances its investments through short-term debt and internally generated cash-flows.

## Arif Habib Limited

Jun-21

Jun-20

Jun-19

12M

12M

12M

**A BALANCE SHEET**

1 Finances	246	53	129
2 Investments	4,852	5,632	4,292
3 Other Earning Assets	2,517	759	432
4 Non-Earning Assets	857	448	789
5 Non-Performing Finances-net	-	-	-
<b>Total Assets</b>	<b>8,472</b>	<b>6,892</b>	<b>5,642</b>
6 Funding	1,847	1,648	669
7 Other Liabilities (Non-Interest Bearing)	1,629	1,978	2,056
<b>Total Liabilities</b>	<b>3,476</b>	<b>3,626</b>	<b>2,725</b>
<b>Equity</b>	<b>4,996</b>	<b>3,266</b>	<b>2,918</b>

**B INCOME STATEMENT**

1 Fee Based Income	1,378	479	679
2 Operating Expenses	(656)	(356)	(397)
3 Non Fee Based Income	1,804	368	(44)
<b>Total Operating Income/(Loss)</b>	<b>2,526</b>	<b>491</b>	<b>238</b>
4 Financial Charges	(133)	(362)	(225)
<b>Pre-Tax Profit</b>	<b>2,393</b>	<b>129</b>	<b>13</b>
5 Taxes	(309)	(69)	(75)
<b>Profit After Tax</b>	<b>2,084</b>	<b>60</b>	<b>(62)</b>

**C RATIO ANALYSIS****1 Business Sustainability**

Pre Tax Margin	173.7%	26.9%	1.9%
EBITDA/ Revenue	183.3%	108.5%	36.3%
Profit / (Loss) Before Interest & Taxes / Total Assets	29.8%	7.1%	4.2%

**2 Financial Sustainability**

Total Investments / Equity	97.1%	172.4%	147.1%
NCB / Equity	38.2%	28.7%	13.9%
LCB/ Total Equity	96.6%	101.0%	102.0%
( Cash & Cash Equivalents + Government Securities ) / Total Assets	38.9%	16.5%	20.8%
Total Debt / Equity	0.1%	25.3%	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

<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 surveill 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>
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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)

### **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

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- (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)
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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)
- (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)

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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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