



The Pakistan Credit Rating Agency Limited

Rating Report

Zafar Securities (Pvt.) Limited | BFR

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Rating History

Dissemination Date	Rating	Outlook	Action	Rating Watch
09-Mar-2023	BFR 3+	Stable	Maintain	-
31-Mar-2022	BFR 3+	Stable	Initial	-

Rating Rationale

Factor	Comment
Ownership	Controlling stake is held by Mr. Syed Asim Zafar, the CEO, with ~80% of the shares while the other directors hold minority shareholding.
Governance	The Company has increased its board size to 5 members with the addition of two non-executive directors, strengthening the governance framework.
Management and Client Services	A lean organizational structure is present with an experienced management team. Client services may be improved with the addition of a research department.
Internal Controls and Regulatory Compliance	Separate internal audit and compliance departments exist; however, increasing the depth of the departments may improve the internal controls framework further.
Business Sustainability	There is product and geographic concentration present in the top line of the Company. ZSPL may look towards diversification to improve its concentration risk.
Financial Sustainability	The equity base of the Company is adequate for its scale of operations. The equity stood at ~PKR 252mln at end-Jun'22 and at ~PKR 249mln at end-Dec'22.

Key Rating Drivers

Zafar Securities (Pvt.) Limited ('ZSPL' or the 'Company') mainly provides equity brokerage services while commodities brokerage is also present. The assigned rating incorporates the business acumen of the primary sponsor. The governance framework has been improved by increasing the board size; however, the addition of independent directors may further enhance governance oversight. ZSPL offers online trading and a mobile app to its customers to facilitate the execution of their transactions. ZSPL managed to contain the decline in traded volumes compared to the market. The brokerage revenue of ZSPL declined by ~25% in FY22 when compared with FY21 despite market volumes declining by ~45% during the same period. The Company is exposed to market risk resulting from proprietary trading and unrealized losses on prop-book amounted to ~PKR 22mln during FY22. Due to losses on the prop book, ZSPL incurred a loss after tax of ~PKR 21mln during FY22. ZSPL has a low-leveraged capital structure with an adequate equity base at end-Dec'22. Going forward, the business environment is expected to remain challenging for the brokerage industry until clarity emerges on the economic front. The rating is dependent on sustainability and improvement in profitability from core income and maintaining market share. Meanwhile, upholding a strong control framework while effectively managing risks, particularly associated with the proprietary investment book is critical.

Disclosure

Name of Rated Entity	Zafar Securities (Pvt.) Limited BFR
Type of Relationship	Solicited
Purpose of the Rating	Broker Fiduciary Rating (BFR)
Applicable Criteria	Methodology Broker Fiduciary Rating(Jan-22)
Related Research	Sector Study Brokerage & Securities(Jan-23)
Rating Analysts	Afnan Iqbal afnan.iqbal@pacra.com +92-42-35869504

Profile

Background Zafar Securities (Pvt.) Limited, “ZSPL or The Company” is a TREC holder of the Pakistan Stock Exchange and a Member of Pakistan Mercantile Exchange Limited. It was incorporated under the Companies Ordinance 1984 in 1999 as a private limited Company.

Operations The Company’s service offering includes Equity Brokerage and commodity brokerage. The clientele of the Company is mainly segmented into three categories i) Retail ii) HNWI and iii) Corporate/Institutional, while corporate clientele makes up a minor part of their customer portfolio.

Ownership

Ownership Structure Controlling stakes are held by the CEO Mr. Syed Asim Zafar at ~80%, The second highest ownership belongs to Ms. Syeda Khola Hussain who owns ~20% of the total shares.

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

Business Acumen The Company’s sponsor possesses the relevant educational background and extensive industry-specific working knowledge. Mr. Syed Asim Zafar has served on the Board of Directors of Lahore Stock Exchange Limited for multiple years from 1994 to 2007. He is also a Founder Member of Pakistan Mercantile Exchange.

Financial Strength The sponsors have adequate net worth and may inject capital into the Company with the increasing quantum of operations.

Governance

Board Structure The Company’s Board of Directors (BoD) is comprised of five members, including the CEO, three of whom are executive and have ownership shares in the Company. The two other directors are non-executives. Independent representation would strengthen the governance factor.

Members’ Profile The board possesses the necessary skills and experience required for capital markets. The board members possess a diversified background in finance and capital markets while also having an entrepreneurial background in the textile industry.

Board Effectiveness To ensure an effective control environment and compliance with reporting standards, the Company has constituted an Audit Committee, HR Committee, and Executive Risk Management Committee. ZSPL also has multiple Management committees including Investment Committee, IT Steering Committee, Web Development & Online Marketing Committee, and the Fraud and Ethics Committee.

Financial The external auditors of the Company are Amin, Mudassar, and Company Chartered Accountants having satisfactory QCR rating from the Institute of Chartered Accountants of Pakistan. The auditors of the Company are classified in the ‘B’ category of the State Bank of Pakistan panel of Auditors.

Management And Client Services

Organizational Structure The Company has a lean organizational structure. ZSPL operates through seven departments namely i) Trading & Settlements ii) Accounts iii) Information Technology iv) Human Resources v) Marketing & Sales vi) Research vii) Internal Audit. All of the departmental heads directly report to the CEO. However, the Internal Auditor reports to the Board’s Audit Committee.

Management Team ZSPL’s management team comprises experienced and professional individuals who possess significant market knowledge. The CFO Mr. Agha Shuja Ali Zaidi has a Master’s Degree and has been overseeing the financial operations for more than 15 years. The head of IT has more than 20 years of industry experience and has been with the Company for more than 16 years.

Client Servicing ZSPL has provided its customers with various channels, including a mobile app and online trading platform to facilitate the execution and monitoring of their transactions.

Complaint Management ZSPL has a feedback area on its website that can be used to lodge complaints and investors can lodge initial complaints through phone calls, SMS/WhatsApp, Email, Website, and by physical appearance; however, the main query system in place for complaints is through their website.

Extent Of Automation / Integration ZSPL has a customized technology-driven trading platform that allows secure trading. ZSPL’s back office and web portal are both purchased from Softech resulting in real-time integration between the two.

Continuity Of Operations ZSPL has in place a comprehensive Disaster Recovery Policy which provides a guide for resuming all critical operations in the shortest possible time. The data pertaining to back-office records and back-office applications are being backed up once a day.

Internal Controls And Regulatory Compliance

Risk Management Framework ZSPL has established Risk Management Committee at the board level for reviewing risk appetite, policies, and controls put in place. ZSPL has an in-house internal audit function comprising a single person. ZSPL has standardized, policy-based risk management procedures.

Regulatory Compliance ZSPL’s compliance department ensures that it is compliant with all the PSX requirements and other regulations (AML/CFT) that pertain to its particular industry, as well as professional standards, accepted business practices, and internal standards.

Business Sustainability

Operating Environment Pakistan's economy is placed at a precarious point right now. The resumption of the IMF program is necessary to have access to much-needed foreign inflows to boost the critically low SBP forex reserves. Inflation has been consistently rising and is forecasted to rise further. The policy interest rates have increased to try and curb inflation, which has impacted the volumes for the brokerage industry as investors are opting for safer fixed-income returns instead of riskier equity investments. Moving forward, resolving the Letter of Credit (LC) issues remains imperative to allow manufacturers to resume their operations and restart the economic activity in the country.

Performance ZSPL's operating revenue is mainly concentrated in equity brokerage while commodities brokerage is also present. Operating revenue comprises commission income and unrealized/realized gain/loss on re-measurement of investments. During FY22, brokerage commission stood at ~PKR 71mln (SPLY: ~PKR 94mln). ZSPL reported a net loss of PKR ~21mln in FY21 compared to a profit of ~PKR 91mln in FY21.

Strategy The management is considering focusing on better integration with technology moving forward. The Company is focusing on enhancing its Retail Clientele by improving its technology integration as well as its social media presence.

Financial Sustainability

Credit Risk As part of its credit policy, ZSPL reviews the withdrawal requests of its clients on a case-to-case basis and checks for any outstanding balances before the withdrawal of funds. Moreover, the Compliance department reviews the creditworthiness of new customers, whereas, KYC and AML policy also exists for further support. A formal credit risk policy should be in place.

Market Risk ZSPL is running a proprietary book with an approximate value of Rs. ~36mln at end-Jun'22. However, it has established an appropriate proprietary trading policy.

Liquidity Risk ZSPL has an adequate liquidity profile. The Company reported current assets of ~PKR 306mln at end-Jun'22 as compared to current liabilities of ~PKR 159mln.

Capitalization The Company has a reasonable capitalization level with regulatory Net Capital Balance (NCB) standing at PKR 99mln at end-Jun'22. The Company has an equity base of ~PKR 252mln at end-Jun'22 (Jun'21: ~PKR 283mln).

PKR mln

Zafar Securities (Pvt.) Limited	Dec-22	Jun-22	Jun-21	Jun-20
	6M	12M	12M	12M

A BALANCE SHEET

1 Finances	-	-	-	-
2 Investments	61	59	82	60
3 Other Earning Assets	70	96	150	59
4 Non-Earning Assets	237	256	373	228
5 Non-Performing Finances-net	-	-	-	-
Total Assets	368	411	605	347
6 Funding	10	10	-	26
7 Other Liabilities (Non-Interest Bearing)	109	149	322	137
Total Liabilities	119	159	322	163
Equity	249	252	283	184

B INCOME STATEMENT

1 Fee Based Income	31	71	94	39
2 Operating Expenses	(44)	(86)	(70)	(58)
3 Non Fee Based Income	10	(4)	65	23
Total Operating Income/(Loss)	(3)	(19)	89	4
4 Financial Charges	(0)	(0)	(0)	(0)
Pre-Tax Profit	(3)	(19)	88	4
5 Taxes	-	(2)	3	(1)
Profit After Tax	(3)	(21)	91	2

C RATIO ANALYSIS**1 Business Sustainability**

Pre Tax Margin	-9.5%	-26.7%	93.7%	9.2%
EBITDA/ Revenue	-2.5%	-19.2%	98.7%	21.7%
Profit / (Loss) Before Interest & Taxes / Total Assets	-0.8%	-4.6%	14.6%	1.0%

2 Financial Sustainability

Total Investments / Equity	24.6%	23.2%	28.9%	32.8%
NCB / Equity	36.7%	39.3%	64.0%	36.2%
LCB/ Total Equity	46.3%	53.4%	62.6%	33.4%
(Cash & Cash Equivalents + Government Securities) / Total Assets	58.6%	66.6%	76.8%	68.4%
Total Debt / Equity	4.0%	4.0%	0.0%	14.0%

Broker Fiduciary Rating Scale & Definitions

An independent opinion on a broker's quality of management and client services, and sustainability of operations

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

<p>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'.</p>	<p>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.</p>	<p>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.</p>	<p>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.</p>	<p>Harmonization A change in rating due to revision in applicable methodology or underlying scale.</p>
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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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(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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(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).

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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)

(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

(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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