RATING REPORT

Next Capital Limited

REPORT DATE:
June 15, 2020

RATING ANALYSTS:

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RATING DETAILS				
	Latest Rating		Previous Rating	
Rating Category	**Long-term**	**Short-term**	**Long-term**	**Short-term**
Entity	A-	A-2	A-	A-2
Rating Outlook	Stable		Stable	
Rating Date	*June 15, 2020*		*April 10, 2019*	

COMPANY INFORMATION	
Incorporated in 2009	**External auditors:** KPMG Taseer Hadi & Co. Chartered Accountants
Public Listed Company	**Chairman of the Board:** Lt. Gen. Tariq Waseem Ghazi (Retd.)
Key Shareholders with stake 10% or more (As of March 2020):	**Chief Executive Officer:** Mr. Muhammad Najam Ali
Mr. Muhammad Najam Ali ~ 27.49%	
Mr. Adnan Afridi ~ 10.59%	

APPLICABLE METHODOLOGY(IES)
VIS Entity Rating Criteria Methodology – Securities Firms Rating (June 2017) ***http://vis.com.pk/docs/Securities%20Firms%20201706.pdf***

Next Capital Limited

OVERVIEW OF THE INSTITUTION	RATING RATIONALE

Next Capital Limited (NCL) was incorporated in 2009 as a public limited company. The company holds a Trading Right Entitlement Certificate (TREC) of Pakistan Stock Exchange (PSX) and is a member of Pakistan Mercantile Exchange (PMEX).

External auditors are 'KPMG Taseer Hadi & Co. Chartered Accountants'. Auditors belong to category 'A' on the approved list of auditors published by the State Bank of Pakistan (SBP).

Profile of Chairman

General Tariq Waseem Ghazi (Ret.) is serving as a chairman of the Board. He was appointed as a secretary of Defense in May 2005 and has also served as chairman of the Civil Aviation Authority, the Fauji Foundation, Defence Housing Authorities, PLA Investments, and as chancellor of Foundation University, Islamabad. Presently, he serves on the boards of Sadiq Public School, Habib University and The Kidney Centre. Mr. Waseem Ghazi a MS degree in War Studies from the University of Islamabad and is a recipient of the Sword of Honour, two international, and fifteen service awards and Hilal-i-

With a decade-long experience, Next Capital Limited (NCL) is primarily engaged in provision of equity brokerage services with presence in money market segment. The company caters to domestic retail and high net worth (HNWI) clients, local institutions and foreign broker dealers. Alongside, it has a reputable market share in investment banking & corporate advisory business in Pakistan. NCL operations are run through its head office and a branch in Lahore.

Key Rating Drivers:

Brokerage industry continues to be affected by economic cycles. Declining trend in trading volumes over the last 2 years has impacted topline of brokerage industry. However, some recovery has been witnessed in the ongoing year.

Performance of the equity market has remained dismal over past two fiscal years (FY18 and FY19) with dwindling trading volumes largely owing to economic slowdown, rising benchmark rate and aggressive foreign selling. However, some recovery has been noted in the ongoing year as reflected by 20% higher brokerage volumes vis-à-vis same period last year.

Industry Trading Metrics	FY17	FY18	FY19	9MFY20	9MFY19
Volume (Ready) (In Billions)	85	43	38	36	30
Value (Regular) (In PKR' Billions)	3,754	2,025	1,551	1,340	1,272

Given tough market conditions during outgoing fiscal year, players with efficient and variable cost structure along with diversified revenue streams managed to remain profitable. Going forward, impact of recently revised brokerage commission structure (a standard range/scale implemented by SECP for all security brokers) and uptick in market volumes in the ongoing year would support profitability profile of brokers. Nonetheless, players with large proprietary book (being exposed to market risk) along with corporate finance & advisory business segment may register the impact of Covid-19 on profitability. In case of prolonged effect of the same on business activity and economic indicators, overall brokerage industry could also face severe adverse impact.

NCL has a diversified revenue mix which provides sustainability to earnings and supports overall business risk profile. Healthy revenues are expected to translate from strong corporate advisory pipeline over the rating horizon.

Overall brokerage income (net of sales tax) grew by ~31% in 9MYF20 as compared to same period last year, mainly on account of management's enhanced focus towards retail business. Proportionate share of retail income in total brokerage revenue has doubled over past three years; the same represents around 66% of total brokerage revenue. Given operational challenges (along with associated settlement risk) as currently faced by industry in the backdrop of covid-19 and its consequent lockdowns, management focus will remain on retail brokerage. Moreover, there are no plans to expand branch network in the short term. Lahore office contributes around one-half of overall brokerage revenues.

Imtiaz for his services to the country.

Profile of CEO

Prior to forming NCL, Mr. Najam Ali served as CEO of JS Investments Limited and served twice as the Chairman of MUFAP. He was also the founding CEO of the Central Depository Company (CDC) and has served on the Board of Directors of Pakistan Oilfields Limited, Askari Bank Limited, KSE, and NCCPL. He is a member of the Institute of Chartered Accountants in England & Wales and Institute of Chartered Accountants of Ontario – Canada. He is a qualified Certified Public Accountant – USA and holds a Bachelor degree in Economics from the University of Michigan, Ann Arbor, USA. Mr. Ali has also attended and successfully completed the 'Advanced Management Program' at the world renowned Harvard Business School, USA. He is currently serving as a member of the Corporate Leaders Advisory Board of Institute of Business Administration (IBA).

Financial Snapshot

Net Equity: Mar'20: Rs. 419.3m, June 2019: Rs. 391.8m

Net Revenue: 9MFY20: Rs. 164.6m, FY19: Rs. 174.3m

Breakup of clients in a tabulated form is shown below:

Number of Clients	FY17	FY18	FY19
Foreign Institutions	5	9	4
Domestic Institutions	153	162	157
Domestic Individuals	711	643	595
Total	**869**	**814**	**756**

International institutional business has declined on a timeline basis (largely due to lower activity by foreign clients and shrinking trading volumes) while domestic institutional business has remained stagnant over the years. Consequently, share contribution of overall institutional customers in total brokerage income has been negatively impacted. Moreover, decline in number of retail clients pertains to closure of accounts due to non-compliance with KYC stipulations.

Strong focus of senior management on advisory business (services including Mergers & Acquisitions, IPOs and Debt & Equity Capital Raising) has resulted in the segment continuing to support overall revenue stream. NCL has adequate signed mandates in hand which would translate in to healthy income for the segment; however, Covid-19 outbreak is expected to impact timeline of realization of these revenues.

Recent uptick in industry trading volumes has improved profitability during 9MFY20. Sizeable jump in other income also supports the overall profitability profile.

After depicting a declining trend over past two years, recurring revenue of the company has improved considerably during 9MFY20 (registering a growth of ~26% vis-à-vis same period last year). Recent growth is on account of increase in other income and higher brokerage revenue which is attributable to improvement in industry trading volumes along with the implementation of minimum brokerage commission by regulator. On the other side, advisory and consultancy business is expected to remain around prior year level.

Given higher liquidity on balance sheets, which is mainly being maintained in the form of placements with banks and exposure margin, and higher benchmark rates mark-up earned on these saving accounts (which is included in other income) has been a major contributor to revenue stream.

On the costs front, effective cost control measures has facilitated in reduction of operational expenses despite higher depreciation charge in the ongoing year. The company's cost-income ratio improved to 78.0% in 9MFY20 from 98.1% in FY18 as increase in operating revenues was higher than operating costs. During 9MFY20, the company reported a profit after tax of Rs. 28.5m (FY19: Rs. 5.3m).

Capitalization indicators have improved in the ongoing year on account of recovery in equity base. Liquidity buffer has also improved.

Equity base had eroded ~16% post FY17; however the same witnessed some recovery at end-9MFY20 on the back of improvement in profitability. The company during outgoing fiscal year obtained a secured credit line of Rs. 250m from Sindh Bank in order to facilitate its working capital requirements. Utilization of the running finance facility, however, has remained low. Leverage indicators have improved at end-9MFY20 while liquid assets coverage of liabilities is considered strong.

Credit risk is considered manageable given one-half of the institutional trades conducted are through Institutional Delivery System (IDS). Furthermore, the company does not take active part in proprietary equity operations, as the portfolio has remained minimal during past few years. NCL has also remained compliant with its overall underwriting limits.

Corporate governance infrastructure
Since last review, senior management team has remained stable except for one change at the position of head of investment banking. Board of Directors (BoD) comprises seven members including Chairman, CEO and five other non-executive directors. Board composition is in compliance with best practices with one-third of board size being represented by independent directors. NCL has been assigned a Broker Management Rating of 'BMR2++' by VIS Credit Rating Company.

Next Capital Limited **Appendix I**

FINANCIAL SUMMARY				*(amounts in PKR millions)*
BALANCE SHEET	**FY17**	**FY18**	**FY19**	**9MFY20**
Trade Debts	428.8	134.0	130.7	98.3
Deposits and Prepayments	281.9	238.4	240.4	99.3
Long Term Investments in PSX Shares	41.2	31.7	14.1	8.5
Proprietary Book	15.4	12.1	34.8	4.0
Cash and Bank balances	269.7	127.0	245.0	276.9
Taxation *(Refundable)*	50.8	54.5	59.6	51.5
Total Assets	1,143.9	697.3	825.9	668.8
Trade and Other Payables	546.4	223.7	225.1	212.6
Long Term Loans *(including lease liability)*	-	-	-	26.4
Short Term Loans – Unsecured	107.3	60.2	200.0	-
Total Liabilities	653.7	287.0	430.9	225.4
Paid up Capital	450.0	450.0	450.0	450,0
Net Worth	465.1	394.7	391.8	419.3
INCOME STATEMENT				
Operating Revenue	353.7	241.1	174.3	164.6
Administrative & Operating Expenses	239.4	240.1	197.6	153.1
Finance Cost	30.1	16.5	6.3	9.4
Profit Before Tax	140.0	4.8	15.7	44.1
Profit After Tax	103.0	(25.3)	5.3	28.5
RATIO ANALYSIS				
Liquid Assets to Total Liabilities (%)	80.7%	124.5%	116.7%	134.5%
Liquid Assets to Total Assets (%)	46.1%	51.2%	60.9%	50.6%
Current Ratio (x)	1.61	2.21	1.71	2.39
Debt Leverage (x)	1.41	0.73	1.10	0.60
Gearing (x)	0.23	0.15	0.51	0.02
Efficiency (%)	70.3%	98.1%	95.1%	78.0%
ROAA (%)	11.4%	-2.8%	0.7%	5.1%
ROAE (%)	31.6%	-5.6%	1.3%	9.4%

ISSUE/ISSUER RATING SCALE & DEFINITIONS Appendix II

VIS Credit Rating Company Limited

RATING SCALE & DEFINITIONS: ISSUES / ISSUERS

Medium to Long-Term

AAA
Highest credit quality; the risk factors are negligible, being only slightly more than for risk-free Government of Pakistan's debt.

AA+, AA, AA-
High credit quality; Protection factors are strong. Risk is modest but may vary slightly from time to time because of economic conditions.

A+, A, A-
Good credit quality; Protection factors are adequate. Risk factors may vary with possible changes in the economy.

BBB+, BBB, BBB-
Adequate credit quality; Protection factors are reasonable and sufficient. Risk factors are considered variable if changes occur in the economy.

BB+, BB, BB-
Obligations deemed likely to be met. Protection factors are capable of weakening if changes occur in the economy. Overall quality may move up or down frequently within this category.

B+, B, B-
Obligations deemed less likely to be met. Protection factors are capable of fluctuating widely if changes occur in the economy. Overall quality may move up or down frequently within this category or into higher or lower rating grade.

CCC
Considerable uncertainty exists towards meeting the obligations. Protection factors are scarce and risk may be substantial.

CC
A high default risk

C
A very high default risk

D
Defaulted obligations

Short-Term

A-1+
Highest certainty of timely payment; Short-term liquidity, including internal operating factors and /or access to alternative sources of funds, is outstanding and safety is just below risk free Government of Pakistan's short-term obligations.

A-1
High certainty of timely payment; Liquidity factors are excellent and supported by good fundamental protection factors. Risk factors are minor.

A-2
Good certainty of timely payment. Liquidity factors and company fundamentals are sound. Access to capital markets is good. Risk factors are small.

A-3
Satisfactory liquidity and other protection factors qualify entities / issues as to investment grade. Risk factors are larger and subject to more variation. Nevertheless, timely payment is expected.

B
Speculative investment characteristics; Liquidity may not be sufficient to ensure timely payment of obligations.

C
Capacity for timely payment of obligations is doubtful.

Rating Watch: VIS places entities and issues on 'Rating Watch' when it deems that there are conditions present that necessitate re-evaluation of the assigned rating(s). Refer to our 'Criteria for Rating Watch' for details. www.vis.com.pk/images/criteria_watch.pdf

Rating Outlooks: The three outlooks 'Positive', 'Stable' and 'Negative' qualify the potential direction of the assigned rating(s). An outlook is not necessarily a precursor of a rating change. Refer to our 'Criteria for Rating Outlook' for details.www.vis.com.pk/images/criteria_outlook.pdf

(SO) Rating: A suffix (SO) is added to the ratings of 'structured' securities where the servicing of debt and related obligations is backed by some sort of financial assets and/or credit support from a third party to the transaction. The suffix (SO), abbreviated for 'structured obligation', denotes that the rating has been achieved on grounds of the structure backing the transaction that enhanced the credit quality of the securities and not on the basis of the credit quality of the issuing entity alone.

(blr) Rating: A suffix (blr) is added to the ratings of a particular banking facility obtained by the borrower from a financial institution. The suffix (blr), abbreviated for 'bank loan rating' denotes that the rating is based on the credit quality of the entity and security structure of the facility.

'p' Rating: A 'p' rating is assigned to entities, where the management has not requested a rating, however, agrees to provide informational support. A 'p' rating is shown with a 'p' subscript and is publicly disclosed. It is not modified by a plus (+) or a minus (-) sign which indicates relative standing within a rating category. Outlook is not assigned to these ratings. Refer to our 'Policy for Private Ratings' for details. www.vis.com.pk/images/policy_ratings.pdf

'SD' Rating: An 'SD' rating is assigned when VIS believes that the ratee has selectively defaulted on a specific issue or obligation but it will continue to meet its payment obligations on other issues or obligations in a timely manner.

REGULATORY DISCLOSURES					Appendix III
Name of Rated Entity	Next Capital Limited				
Sector	Brokerage				
Type of Relationship	Solicited				
Purpose of Rating	Entity Rating				
Rating History	**Rating Date**	**Medium to Long Term**	**Short Term**	**Rating Outlook**	**Rating Action**
			RATING TYPE: ENTITY		
	19-Jan-16	A-	A-2	Stable	Initial
	19-Mar-18	A-	A-2	Stable	Reaffirmed
	10-Apr-19	A-	A-2	Stable	Reaffirmed
	15-June-20	A-	A-2	Stable	Reaffirmed
Instrument Structure	N/A				
Statement by the Rating Team	VIS, the analysts involved in the rating process and members of its rating committee do not have any conflict of interest relating to the credit rating(s) mentioned herein. This rating is an opinion on credit quality only and is not a recommendation to buy or sell any securities.				
Probability of Default	VIS' ratings opinions express ordinal ranking of risk, from strongest to weakest, within a universe of credit risk. Ratings are not intended as guarantees of credit quality or as exact measures of the probability that a particular issuer or particular debt issue will default.				
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