

RATING REPORT

Adam Securities Limited

REPORT DATE:

July 26, 2019

RATING ANALYSTS:

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RATING DETAILS

Rating Category	Latest Rating		Previous Rating	
	Long-term	Short-term	Long-term	Short-term
Entity	BBB	A-3	BBB-	A-3
Rating Outlook	Stable		Stable	
Rating Date	July 26, 2019		March 30, 2018	

COMPANY INFORMATION

Incorporated on 9 th June 2001	External auditors: M/s Baker Tilly Mehmood Idrees Chartered Accountants
Public Un-listed Company	Chairperson of the Board: Mr. Noman Abdul Majeed Adam
Key Shareholders (with stake 5% or more):	Chief Executive Officer: Mr. Noman Abdul Majeed Adam
Noman Abdul Majeed Adam – 51% Abdul Majeed Adam – 49%	

APPLICABLE METHODOLOGY(IES)

VIS Entity Rating Criteria Methodology – Securities Firms Rating (May 2015)

<http://www.jcrvis.com.pk/Images/Securities%20methodology%201%20-2015.pdf>

Adam Securities Limited

OVERVIEW OF THE INSTITUTION

RATING RATIONALE

Adam Securities Limited (ASL) is a public unlisted company which was incorporated in June 2001 under the Companies Ordinance 1984. ASL primarily undertakes equity brokerage; it is a TREC holder of Pakistan Stock Exchange.

Profile of Chairman & CEO

Mr. Noman Abdul Majeed is the CEO and Director of the company with over 10 years of experience in Stock Market, International Markets and Commodities Market. He is the head of Security Brokerage Division of the company as well. Mr. Noman holds a graduate degree from University of Karachi.

Adam Securities (ASL) was incorporated in 2001 as a private limited company but later changed its status to public unlisted company in 2016. ASL is principally engaged in provision of equity brokerage facilities to domestic retail and institutional clients. Shareholding of the company is primarily vested with two individuals including the CEO.

Rating Drivers

Brokerage industry continues to be affected by economic cycles. Declining trend in trading volumes during FY18 and ongoing year has impacted the topline of brokerage industry.

Political uncertainty due to elections, aggressive foreign selling, rising current account deficit and expected slow-down in GDP growth has translated into dismal performance of the benchmark index over the last 18 months. Resultantly, market volumes have posted a noticeable decline during the period. Going forward, market volumes, over the short-term, are expected to remain under pressure given rising interest rates and risk of rupee depreciation. 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.

Downward momentum in brokerage volumes has pushed down earnings profile.

Given industry-wide drop in trading volumes, ASL’s brokerage commissions have also been impacted; in FY18 these dropped by 17% whilst in the latest 9 month period the revenues were 44% lower than corresponding period last year. The drop in commission revenues is mainly attributable to lower trading volumes, as commission per share depicted an improvement on a timeline. Overall, ASL’s commission per share and quantum of clientele remains the lowest amongst peers.

Precipitated by the drop in trading volumes and lower one-off capital gains, ASL’s operating profit dropped by 70% in FY18, whilst they further dropped by another 23% in 9MFY19 vis-à-vis corresponding period last year. Nevertheless, given a very lean expense base, the company’s operations remained profitable. On the contrary, on a YoY basis, the efficiency ratio actually depicted an improvement dropping to 91% (FY17: 100%), which compares favorably to peers. Even though ASL’s RoAA has depicted volatility given the drop in industry-wide profitability, the RoAA for FY18 remained positive unlike other industry participants, of which 7 of 13 were in losses (VIS Rating Universe). Nevertheless, the negative momentum in earnings profile is expected to continue, with pre-tax profits dropping by 38% in FY18 and 28% in 9MFY19 vis-à-vis corresponding period last year.

Ratings can benefit from diversification of revenues

In order to reduce its reliance on brokerage volumes, ASL has initiated 2 new business lines of corporate finance advisory and commodities. Significant contribution from these newly initiated lines of business will help in revenue diversification, which is warranted.

Liquidity profile is considered adequate while credit risk and market risk remains manageable

Liquid assets are more than sufficient to account for current liabilities of the company as liquid assets in relation to total liabilities increased to 253.4% at end-9MFY19 (FY18: 183.5%; FY17: 140.1%). On the other hand credit risk for ASL is deemed to be on the lower side as major quantum of trade receivables are due within 3 months and receivables against margin financing have declined on the back of reduced market activity. Moreover market risk emanating from the investment portfolio is considered limited as most of the proprietary book is invested in futures market.

Capitalization indicators are supported by low leveraged capital structure and high profit retention

Equity base of the company has improved on a timeline basis on account of consistent profitability and a conservative payout policy. In addition, equity injection of Rs. 15m has been undertaken in the ongoing fiscal year, which has increased the paid up capital to Rs. 265m (FY18: Rs. 250m). Capitalization derives strength from no outstanding interest bearing debt on the balance sheet. Debt leverage is also on the lower side and has been decreasing on a timeline basis (9MFY19: 0.21x; FY18: 0.38x; FY16: 0.58x).

Corporate Governance framework has room for improvement

Current composition of the Board of Directors comprises of 3 members; 2 executive directors and 1 independent director. The position of CEO and Chairman is currently not segregated. The management has planned to further improve the corporate governance structure by appointing an independent director as the chairman of the board in the upcoming elections. However the governance structure in terms of composition of BoD members, size of the board and female representation is not adequate. Also constitution of Risk Management Committee and Board Audit Committee may further improve board level governance. On the flip side ASL upgraded its external auditors from category 'B' to category 'A' which depicts improvement in the overall governance framework.

FINANCIAL SUMMARY (amounts in PKR millions)			
BALANCE SHEET			
	30-Jun-17	30-Jun-18	31-Mar-19
Trade Debts	218.2	17.3	74.0
LT Investments	49.6	29.8	26.2
ST Investments (Prop book)	9.9	121.0	237.1
Cash and Bank balances	53.8	37.0	43.9
Total Assets	885.9	787.3	764.7
Trade and Other Payables	72.4	77.3	70.9
Short Term Financing	20.7	-	-
Net Worth	540.4	557.9	619.5
INCOME STATEMENT			
	30-Jun-17	30-Jun-18	31-Mar-19
Total Revenue	175.9	111.4	76.3
Brokerage Income	90.7	75.7	34.9
Corporate Advisory Income	0.6	7.6	1.7
Administrative Expenses	(95.5)	(86.9)	(55.8)
Finance Costs	(8.3)	(3.4)	(2.0)
Profit Before Tax	113.1	70.6	47.1
Profit After Tax	86.2	17.6	46.6
RATIO ANALYSIS			
	30-Jun-17	30-Jun-18	31-Mar-19
Market Share (Share Turnover) (%)	11.8%	12.6%	N/A
Commission Income / Turnover (Paisa/Share)	0.90	1.39	N/A
Liquid Assets to Total Liabilities (%)	140.1%	183.5%	253.4%
Liquid Assets to Total Assets (%)	49.6%	49.6%	43.8%
Debt Leverage (x)	0.58	0.38	0.21
Gearing (x)	0.04	-	-
Efficiency (%)	99.9%	91.0%	107.1%
ROAA (%)	11.9%	4.0%	7.9%
ROAE (%)	18.2%	3.2%	10.5%

ISSUE/ISSUER RATING SCALE & DEFINITIONS

Appendix II

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

Rating Watch: JCR-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.jcrvis.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.jcrvis.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

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.

and not on the basis of the credit quality of the issuing entity alone.

'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.jcrvis.com.pk/images/policy_ratings.pdf

'SD' Rating: An 'SD' rating is assigned when JCR-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	Adam Securities 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				
	26-July-2019	BBB	A-3	Stable	Upgrade
	30-March-2018	BBB-	A-3	Stable	Upgrade
	31-October-2017	BB+	A-3	Stable	Upgrade
	03-April-2017	BB	A-3	Stable	Reaffirmed
	30-Dec-2015	BB	A-3	Stable	Initial
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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