

RATING REPORT

Dawood Equities Limited

REPORT DATE:

June 29, 2017

RATING ANALYSTS:

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RATING DETAILS

| Rating Category | Latest Rating | | Previous Rating | |
|-----------------|---------------|------------|-----------------|------------|
| | Long-term | Short-term | Long-term | Short-term |
| Entity | BB- | A-3 | BB+ | A-3 |
| Rating Outlook | Stable | | Stable | |
| Rating Date | Jun 23, 2017 | | Dec 15, 2015 | |

COMPANY INFORMATION

| | |
|---|---|
| Incorporated in 2006 | External auditors: M/s Haroon Zakaria & Co. Chartered Accountants |
| Listed Public Limited Company | Chairman of the Board: Mr. Junaid Zakaria Dada |
| Key Shareholders (with stake 5% or more): | Chief Executive Officer: Mr. Abdul Aziz Habib |
| Mr. Ayaz Dawood – 19.3% | |
| Bank of Khyber – 15.0% | |
| Mr. Asim Abdul Ghani – 10.1% | |
| B.R.R. Guardian Modaraba – 7.2% | |

APPLICABLE METHODOLOGY(IES)

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

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

Dawood Equities Limited

OVERVIEW OF THE INSTITUTION

RATING RATIONALE

Dawood Equities Limited (DEL) is a listed public limited company. It is principally engaged in provision of equity brokerage services to domestic clients. The company commenced operations in 2006.

Profile of CEO

Mr. Abdul Aziz Habib possesses more than a decade of experience in textile exports and has a degree in Master of Arts (M.A.) Economics.

Financial snapshot

9MFY17: Total Equity: Rs. 286.7m

9MFY17: Profit after Tax: Rs. 44.0m

Incorporated in 2001, Dawood Equities Limited (DEL) is engaged in provision of equity brokerage services to domestic retail and institutional clients along with high net worth individuals (HNWIs). In 2015, the company also initiated underwriting activities. Majority stake of DEL is held by First Dawood Group (FDG), a conglomerate having presence in the financial sector. FDG holds 25% stake in the company while remaining shareholding is represented by Bank of Khyber, various financial institutions and general public. The company operates through its head office and two branches in Karachi and Hyderabad, Sindh.

Rating drivers

- Corporate Governance & Internal Control:** Assigned ratings take into account notable weaknesses in internal control and governance framework of the company. Since last review, DEL has been non-compliant with regulations in several instances. Given the nature of these breaches, ability of the company to manage credit risk is considered to be weak. An internal audit & compliance resource was deployed at the company in the outgoing year. However, scope of audit is limited to operational processes. In order to mitigate risk of regulatory breaches, strengthening of internal control and compliance framework is warranted.
- Capitalization & Liquidity:** Given the additional inflow as a result of company's divestment in PSX shares; net worth of DEL increased to Rs. 286.7m at end-1Q17. However, equity base remains on the lower side in relation to peers. The company underwrote several transactions during period under review; further growth in underwriting activity is envisaged by management in the ongoing fiscal year. With equity base standing on the lower side in relation to peers, underwriting capacity of the company remains constrained. Moreover, receivables from brokerage operations are heavily concentrated among top 10 debtors indicating considerable credit risk.
- Profitability:** Profitability has depicted modest growth on the back of increase in brokerage commission earned. Brokerage income augmented as a result of higher commission generated from individual clients; this accounted for around half of revenue base. Recurring income comfortably covers operating expenses of the company as indicated by an efficiency ratio of 21.5% with it comparing most favorably amongst peers. In line with approved plans, new HNWI clients were added to the customer base during period under review and management's focus is expected to remain in the same direction for the ongoing year.
- Investments:** Short term investments depicted a decline at end-1HFY17; though increasing by a sizeable quantum at end-March 2017 on account of notable related party exposure. Market risk emanating from investment portfolio is considered manageable as it accounts for less than 2% of total equity. Going forward, DEL intends to hold liquid shares which can be pledged against clients' margin trades.

| FINANCIAL SUMMARY (amounts in PKR millions) | | Appendix I | | |
|--|------------------|-------------------|------------------|--|
| BALANCE SHEET | 31-Dec-16 | 30-Jun-16 | 30-Jun-15 | |
| Trade Debts | 98.5 | 90.4 | 75.3 | |
| Deferred Tax | 35.3 | 37.2 | 35.0 | |
| Long Term Investments | 68.9 | 40.2 | 40.4 | |
| Short Term Investments (Prop. Book) | 19.4 | 18.4 | 29.3 | |
| Cash and Bank balances | 3.0 | 12.5 | 6.1 | |
| Total Assets | 290.1 | 240.3 | 258.7 | |
| Trade and Other Payables | 28.1 | 16.8 | 36.0 | |
| Short Term running finance | - | - | - | |
| Accumulated (Loss)/profit | (95.5) | (105.3) | (106.3) | |
| Net Worth | 262.0 | 223.5 | 222.7 | |
| INCOME STATEMENT | | | | |
| | 31-Dec-16 | 30-Jun-16 | 30-Jun-15 | |
| Brokerage Income | 12.1 | 15.1 | 13.5 | |
| Recurring Income | 34.6 | 32.5 | 28.3 | |
| Operating Revenue | 34.2 | 30.5 | 26.6 | |
| Administrative Expenses | 7.4 | 12.6 | 10.4 | |
| Finance Costs | 0.0 | 0.1 | 0.1 | |
| Profit Before Tax | 13.9 | (0.5) | 13.3 | |
| Taxation | (4.1) | 1.5 | 33.3 | |
| Profit After Tax | 9.7 | 1.0 | 46.6 | |
| RATIO ANALYSIS | | | | |
| | 31-Dec-16 | 30-Jun-16 | 30-Jun-15 | |
| Commission Income / Turnover (Paisa/Share) | 3.78 | 3.81 | 2.10 | |
| Liquid Assets to Total Liabilities | 47.5% | 156.5% | 60.1% | |
| Debt Leverage (x) | 0.11 | 0.07 | 0.16 | |
| Gearing (x) | - | - | - | |
| Efficiency (%) | 21.5% | 38.7% | 36.7% | |
| ROAA (%) | 7.3% | 0.4% | 19.6% | |
| ROAE (%) | 8.0% | 0.5% | 23.4% | |

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

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: 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

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 | Dawood Equities 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 |
| | <u>RATING TYPE: ENTITY</u> | | | | |
| | 23-Jun-17 | BB- | A-3 | Stable | Downgrade |
| | 15-Dec-15 | BB+ | A-3 | Stable | Initial |
| Instrument Structure | N/A | | | | |
| Statement by the Rating Team | JCR-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 | JCR-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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