



CONSTRUCTION

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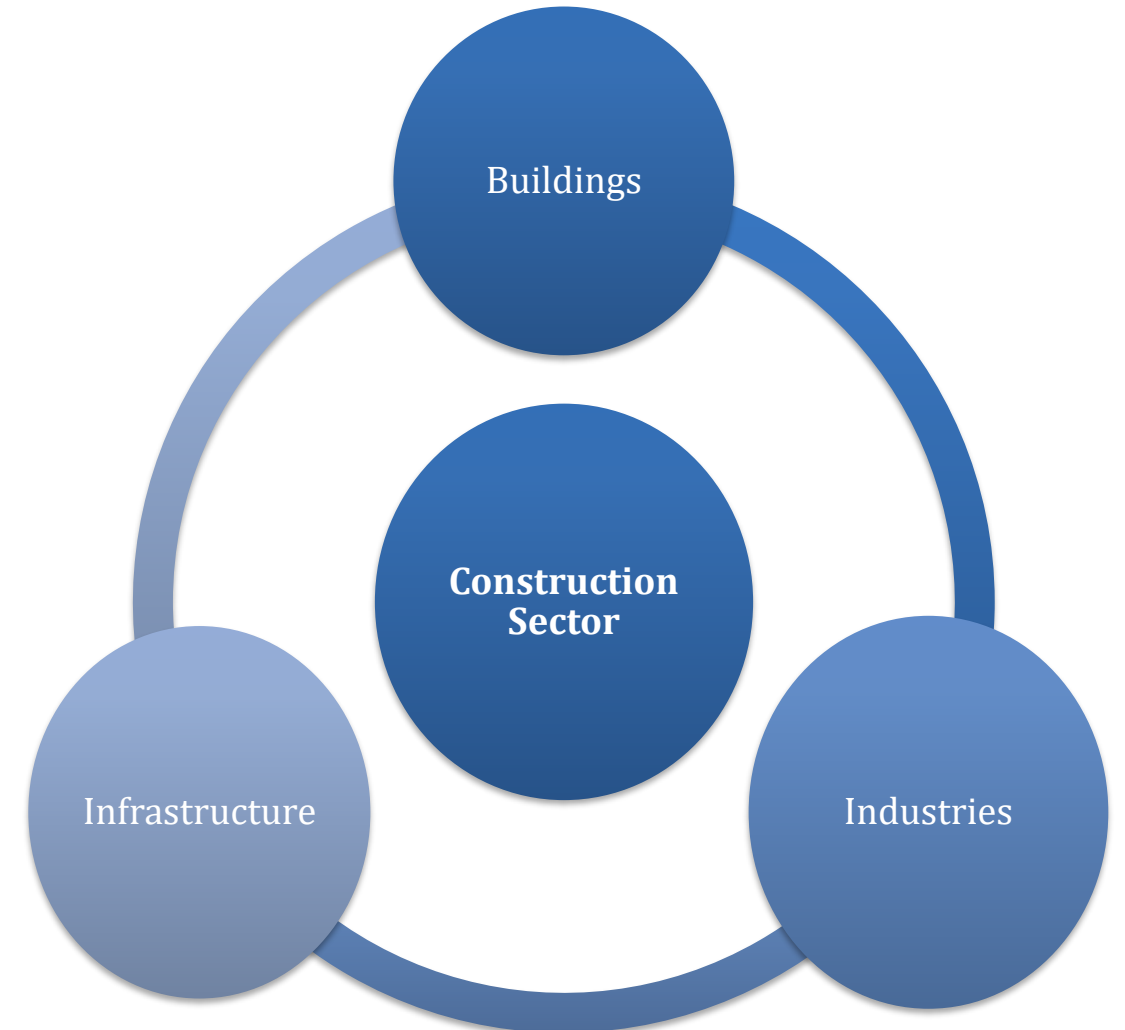


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Construction

Global | Overview

- Construction comprises all economic activities directed to the creation, renovation, repair or extension of fixed assets in the form of buildings, land improvements of an engineering nature, and other engineering constructions such as roads, bridges, dams and so forth.
- The global construction sector is a rapidly growing sector where its market value is expected to increase from USD~15.2trn in CY23 to USD~16.0trn in CY24, with a compound annual growth rate (CAGR) of ~5.1%.
- Additionally, the sector’s market size is forecast to reach USD~19.9trn by CY28, with a CAGR of ~5.6% owing to urbanization, population growth, government support, industrial development, and the rise of smart cities.
- The construction sector can be broadly classified into the following segments:
 - a) Buildings
 - b) Infrastructure
 - c) Industries
- Global construction sector is of major economic significance, as it contributed ~14.3% to the global GDP in CY23 and employed ~220mln people across the globe (~2.8% of global population).



Construction

Global | Overview

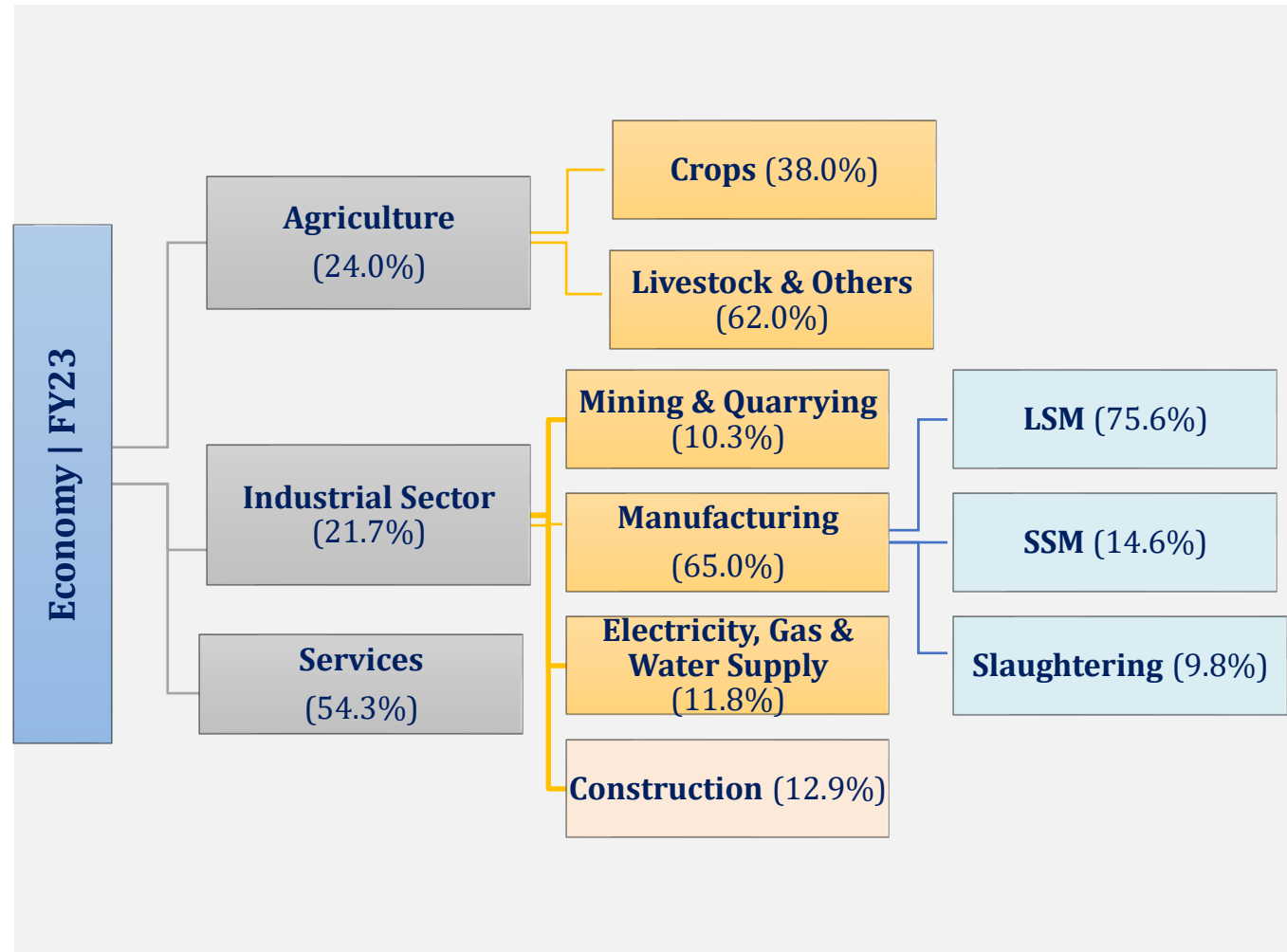
- Construction is primarily driven by infrastructure demand arising from level of economic activity, population growth and population income levels. Residential buildings contributed ~40.9% to global construction sector in CY22, followed by Non-Residential building (~26.6%) and civil engineering (~32.6%).
- In CY22, Asia's population formed ~30% of the global total and the fastest growing GDP averaging at ~2.9% led the global construction activities, particularly in China, as ~8 of the top 10 global construction firms are located there. Meanwhile, output from construction activities contributed ~6.9% to their GDP in CY22.
- Overall, Asia contributes to ~48.8% of global construction activity during the year, followed by Europe (~25.6%), America (~22.2%) and Middle East & Africa (~3.5%).
- Due to high linkages of construction sector with other allied industries, the growth in construction sector bodes well for the overall growth of the economic activity.
- However, global construction activity is forecast to decline by ~0.3% in CY24 to record at USD~9.6tn. Input cost inflation and tighter credit conditions are likely to weigh on demand contraction.
- The ongoing real-estate downturn in China continues to shape the global narrative into CY24, although some rebound in construction activity in the country is expected by CY25.

Top 10 Players CY22 Revenue (USD bln)			
Sr.	Company	Country	Revenue
1	China Construction Engineering Co. Ltd.	China	305.6
2	China Railway Group Ltd.	China	171.7
3	China Railway Construction Corporation Ltd.	China	163.0
4	China Communication Construction Group Ltd.	China	94.3
5	Metallurgical Corporation of China Ltd.	China	88.1
6	Power Construction Corporation of China	China	85.0
7	Vinci	France	65.0
8	China Energy Engineering Corporation	China	54.1
9	Bouygues	France	46.7
10	Shanghai Construction Group	China	42.5
Total			1,116

Construction

Local | Overview

- In FY23, Pakistan's GDP (nominal) stood at PKR~79.7trn (FY22: PKR~63.3trn), contracting, in real terms, by ~0.17% YoY (FY22: ~6.3% growth). Industrial activities in FY23 held ~21.7% share in the GDP while the manufacturing activities made up ~65% of the value addition.
- The GDP growth rate of ~1.0% in real terms for 2QFY24 signals a deceleration in comparison to SPLY and 1QFY24 when real GDP growth rate stood at ~2.2% and ~2.5%, respectively.
- Large Scale Manufacturing (LSM) in Pakistan is essential for the economic growth considering its linkages with other sectors, as it represented ~75.6% value of all manufacturing activities in FY23. The LSM fell by ~10.3% in FY23 (FY22: ~11.7%) However, it increased by ~0.5% YoY in 7MFY24 period.
- The Construction sector is classified under the Industrial Activities segment of the economy. In 2QFY24, the sector experienced a negative growth of ~17.6% (2QFY23: ~-5.0%; 1QFY24: ~0.7%). In 1QFY24, the sector contributed ~11.5% in Industrial Activities (1QFY23: ~12.1%) and ~2.7% to GDP (at current prices) (1QFY23: ~2.7%).



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Local | Overview

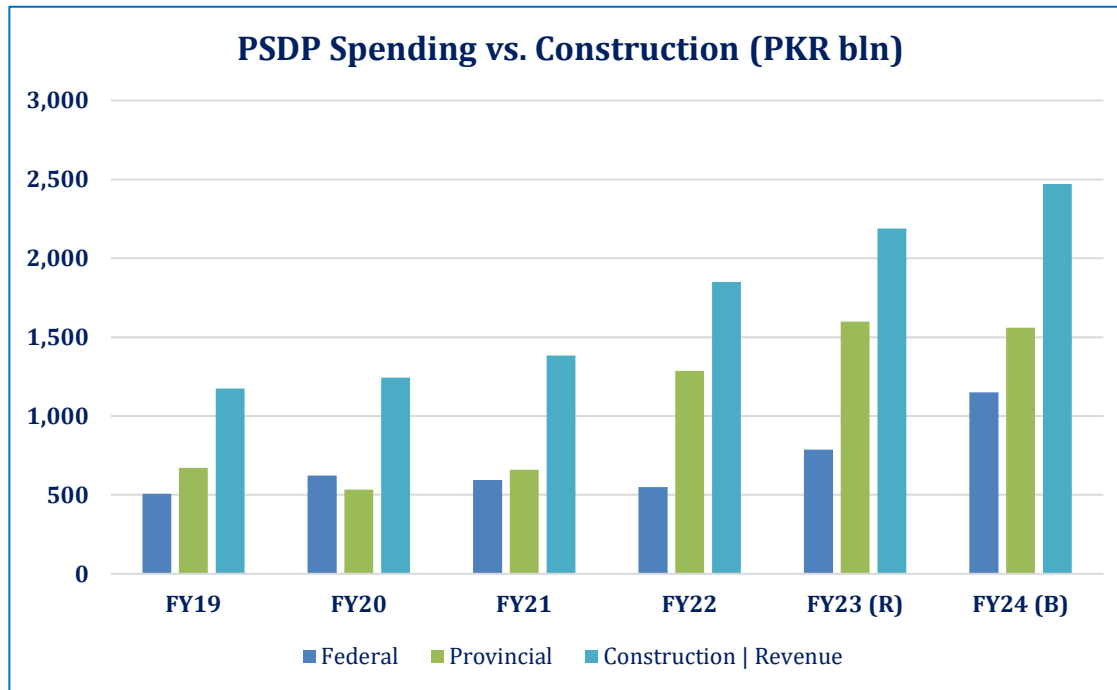
- During FY23, despite the sector recording ~18.4% YoY growth in terms of market size, its share in Industrial activities was down to ~12.5% (SPLY: ~13.6%). This decline was attributed to factors like increases in input prices and wages, higher borrowing cost, and slower growth in development spending.
- Moreover, the floods of Jul-Aug'22, expiry of amnesty schemes, and constraints in fresh disbursements in subsidized lending schemes such as Mera Pakistan Mera Ghar scheme also adversely impacted the sector.
- Meanwhile, the ~9.4% dip in Construction GFCF resulted on the back of lower machinery imports in the wake of SBP-imposed imports restrictions during May'22-Jun'23 (machinery imported for public works and building registered ~64.7% YoY decline). These were later lifted in Jun'23.
- In 7MFY24, production of cement, glass plates and sheets and steel products (including long and flat) registered ~(0.1)%, ~3.5% and ~0.5% YoY growth, respectively. In 1HFY24, however, construction exhibited ~17.6% YoY decline.
- Over ~10,000 firms are registered with the Pakistan Engineering Council as constructors/ contractors. However, only ~156 (~1.6%) of these hold the CA category (no limit on cost of construction project) license which enables them to be on the pre-qualifying list of approved constructors.

Particulars	FY19	FY20	FY21	FY22	FY23
Contribution to GDP (%)	2.9%	2.8%	2.7%	2.9%	2.8%
Market Size (PKR bln)	1,175	1,243	1,383	1,850	2,190
YoY Growth (%) Market Size	-8.8%	5.8%	11.3%	33.8%	18.4%
Gross Fixed Capital Formation (GFCF) (PKR mln)	44,489	50,961	50,710	95,807	76,967
YoY Growth (%) GFCF	-47.7%	-40.0%	-40.3%	12.7%	-9.4%
Labor Force (mln No.)	5.2		6.4		
Association	Pakistan Engineering Council (PEC)				

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Local | Demand

- A major driver of demand comprises the Public Sector Development Program (PSDP) expenditure, followed by Private Investments in the construction sector. The PSDP FY24 has been aligned towards the 5Es (exports, equity, empowerment, environment and energy) and 4 RF (Resilient Recovery, Rehabilitation and Reconstruction Framework) to regain economic growth.
- PSDP FY24 was up ~30.7% YoY, recording at PKR~950bln. During 7MFY24, PKR~372bln has been authorized, with total expenditure amounting to PKR~161.7bln. Moreover, the Budget FY24 has envisaged, under Current and Development Expenditure on Revenue Account, amounts of PKR~40.5bln and PKR~39.1bln on account of Construction & Transport (SPLY: PKR~30.2bln and PKR~55.2bln, respectively)*.



Federal Ministries	FY24		FY23	
	PKR mln	% Share	PKR mln	% Share
Provinces & Special Areas	167,900	18%	140,635	19%
National Highways & Railways	157,500	17%	117,253	16%
Water Resources	107,500	11%	97,559	13%
Education	68,200	7%	51,959	7%
Power (NTDC/ PEPCO)	54,550	6%	42,683	6%
Housing	40,680	4%	17,729	2%
Railways	33,000	3%	32,648	4%
Planning, Development & Special Initiatives	24,897	3%	37,177	5%
National Health Services	13,100	1%	12,651	2%
Science & Technology Research	8,000	1%	5,716	1%
Others	274,673	29%	170,990	24%
Total Federal PSDP	950,000	100%	727,000	100%

Note: Education includes HEC as well as Federal Education & Professional Training. NHA is classified under Corporations. * FY23 revised figures were PKR~30.8bln and PKR~16.0bln, respectively.

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Local | Major Water Sector Projects (FY23)

Project	Location	Approx. Cost (PKR mln)	Live Storage	Irrigated Area	Status
Diamer Basha Dam (Dam Part only)	KP & GB	479,686.0	6.4MAF	1.23mln acres	ECNEC approved dam part of the project on 14-11-2018 (out of PKR~479bln, PKR~237bln will be federal grant, PKR~144bln commercial financing, PKR~98bln WAPDA equity). Physical progress is ~9%.
Mohmand Dam Hydropower Project (800 MW)	Mohmand District, KP	114,285.0 (dam part Cost)	0.676 MAF	16,737 acres	Phase-I ECNEC approved on 30-06-2018 at a total cost of PKR~309.6bln (dam part+ power generation cost). Physical progress is 20.4%.
Kachhi Canal (Phase-I)	Balochistan	80,352.0	-	7,200 acres	Phase-I completed. Out of ~102,000 acres CCA about ~57,000 acres developed in Dera Bugti, Balochistan. However, command area of remaining works has not yet been developed. Physical progress is 99.9%.
Nai Gaj Dam	Dadu, Sindh	46,980.0	160,000 (acre feet)	28,000 acres	Physical Progress 42.8%.
KurramTangi Dam (PhaseI, Kaitu Weir)	KP	21,059.0	0.9MAF	16,000 acres	Physical Progress 64.7%.
Naulong Dam	JhalMagsi, Balochistan	39,900.0	0.20 MAF	47,000 acres	Updated 2 nd revised PC-I approved by ECNEC on 07.10.2022. Physical Progress 1.8%.

Construction

Local | Major Water Sector Projects (FY23)

Project	Location	Approx. Cost (PKR mln)	Live Storage	Irrigated Area	Status
Mangi Dam Project	Khost River, Quetta Balochistan	13,248.0	29,509.8 (acre feet)	8.1 MGD	Revised PC-I approved on 06.07.2022. Physical Progress 57.3%.
Hingol Dam	Lasbela, Balochistan	421.4	0.82 (MAF)	65,000 acres	Detailed Engineering Design is in progress. 16% progress achieved.
Murunj Dam	Rajanpur, Punjab	350.0	0.6	12,000 acres	Feasibility study progress is 90%.
Sindh Barrag	Thatta, Sindh	327.5	1.8MAF	-	Feasibility study progress is 96%.
K-IV Greater Water Supply Scheme	Sindh	126,000.0	-	260MGD	Physical progress 1.0%.
Chashma Right Bank Canal (CRBC) Lift-cum-Gravity	KP	189,606.4	-	286,100 acres	ECNEC approved the PC-I on 07.10.2022.
Restoration/ Revamping (R/R) of Gujjar Nullah	Sindh	14,854.0	-	To mitigate urban flooding in	Physical Progress 80%. Financial Progress 85.8% as per revised approved PC-I.
R/R Nurangi Nullah	Sindh	15,007.3	-	Karachi	Physical Progress 75%. Financial Progress 90.8% as per revised approved PC-I.

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Local | Infrastructure Development

- With respect to Punjab, during FY23, Infrastructure projects included in Annual Development Plan comprised ~12 Roads and Bridges, ~21 irrigation projects and ~17 urban development and transport initiatives. To name a few, these included the following:
 - Chief Minister Punjab's Road Rehabilitation Programme
 - Sialkot and Multan Ring Road projects
 - Improvement / Rehabilitation of Rawalpindi – Murree – Kashmir (RMK) road, Length ~38Km
 - Construction of Flood bund from Hairo Flood Bund to Raikh Baghwala Flood Bund on Right Side of River Indus
 - Construction of Jalapur irrigation project and its system
 - Construction of Flyover & At-grade Improvement at Shahkam Chowk, Lahore (1st Revised)
 - Construction of Underpass at Ghulab Devi Hospital and additional lanes on Lahore Bridge
 - Construction of Sheranwala Flyover, Lahore

- The Annual Development Plan for FY24 includes ~10 Roads and Bridges and ~11 urban development and transport initiatives, along with construction of Energy Efficient building using indigenous resources.

- Moreover, under PSDP 2023-24, PKR~2,900mln have been allocated to ~14 ongoing schemes, total cost of which stands at PKR~16,000mln. One additional scheme, namely, Acquisition of Land for Establishment of SME facilitation centers at various locations, has been envisioned for the ongoing FY24, budgeted PSDP allocation of which is PKR~100mln, while approved cost stands a PKR~1,250mln.

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Local | Transport Infrastructure under CPEC

- In addition to the transport infrastructure projects falling under the CPEC ambit (enlisted below), ~08 are in the pipeline, including Dir Expressway and Peshawar-D.I.Khan Motorway, while ~05 are long-term projects, including Karachi Circular Railway and Mirpur-Muzaffarabad-Mansehra Road, to name a few.

Completed Projects	Length (KM)	Location	Approx. Cost (USD mln)
KKH Phase II (Havelian-Thakot section)	120	KP	1,315
Peshawar-Karachi Motorway (Multan-Sukkur Section)	392	Punjab, Sindh	2,889
Orange Line Metro Train - Lahore	27	Punjab	1,626
Cross Border Optical Fiber Cable (Khunjrab - Rawalpindi)	820	KP, Punjab	44
Pilot Project of Digital Terrestrial Multimedia Broadcast (DTMB)	-	Punjab	4.0
Hakla - D.I Khan Motorway	297	Punjab	PKR~122,181mln
Under Construction Projects	Length (KM)	Location	Approx. Cost (PKR)
Zhob - Quetta (Kuchlak) (N-50)	305	Baluchistan	PKR~66,833mln.
Khuzdar-Basima Road (N-30)	106	Baluchistan	PKR~20bln
Hoshab - Awaran Road Section (M-8)	146	Baluchistan	PKR~26bln
KKH Alternate Route Shandur - Chitral Road	153	KP	PKR~16bln
Nokundi-Mashkhel Road	103	Baluchistan	PKR~16bln

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Local | Gwadar Projects under CPEC

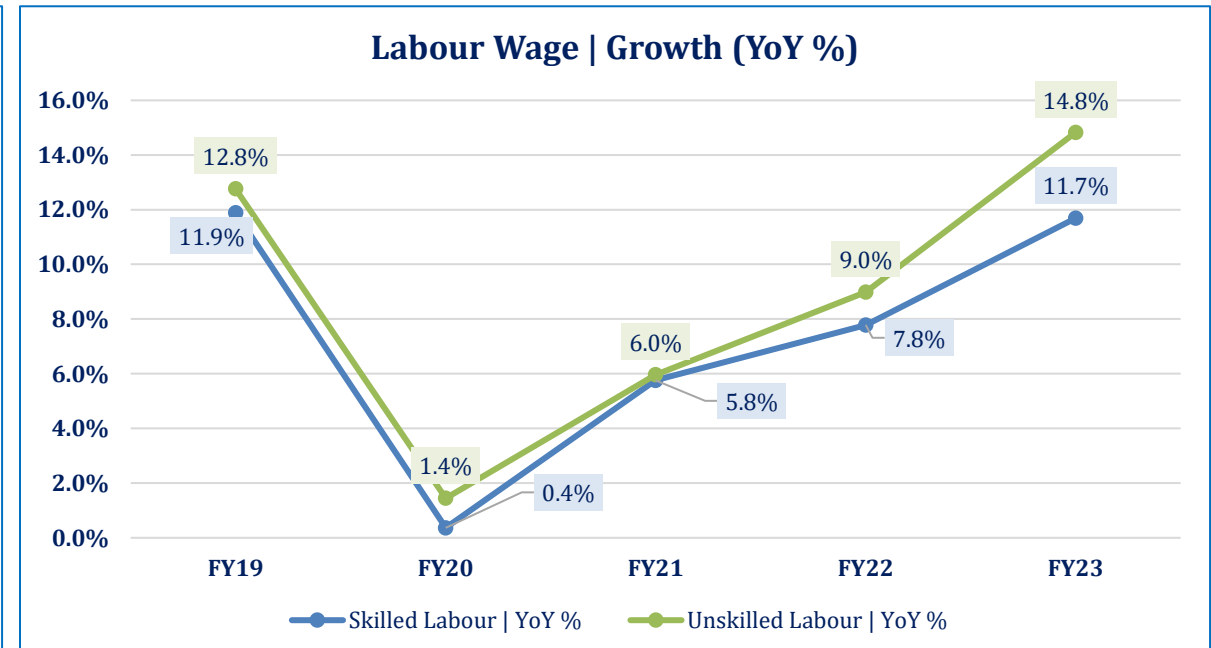
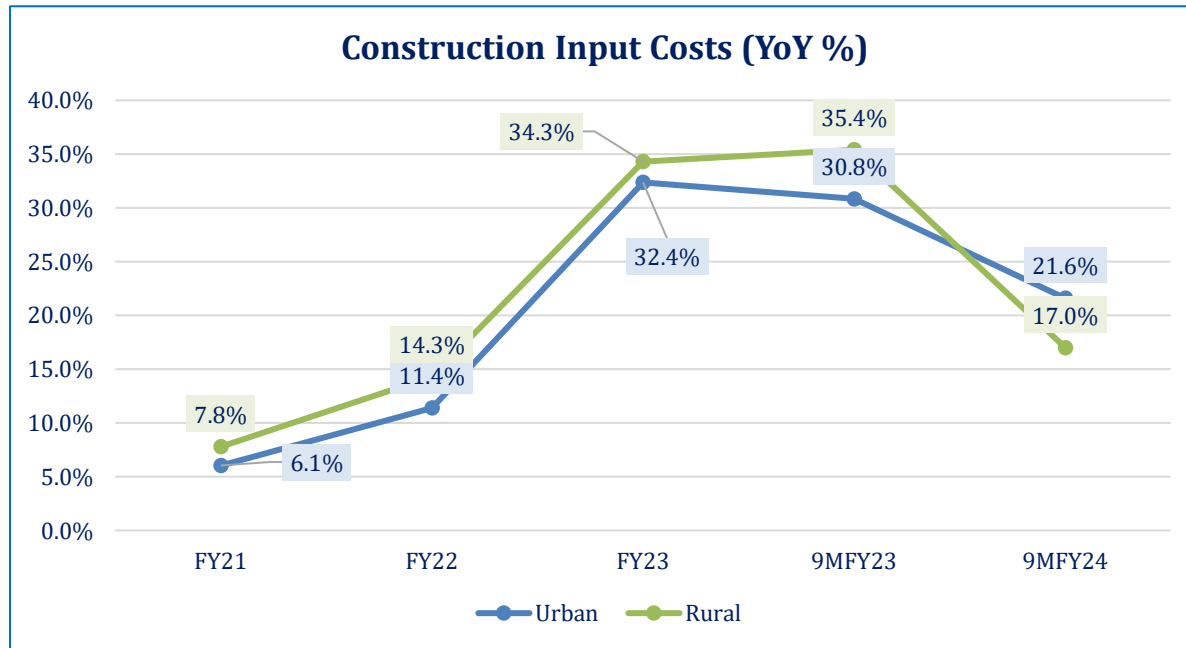
- In addition to enlisted on the right, ~04 are in the pipeline, including Gwadar Smart Environment Sanitation System and Landfill Project.

Completed Projects	Length (KM)/ Area (acres)	Approx. Cost (USD mln)
Development of Port and Free Zone	2,281 acres	300
Gwadar Smart Port City Master Plan	-	04
Pak-China Technical and Vocational Institute at Gwadar	-	10
Gwadar Eastbay Expressway	-	179
Pak-China Friendship Hospital	-	100
1.2 MGD Desalination Plant	-	12.7
Under Construction Projects	Length (KM)	Approx. Cost (USD, PKR)
New Gwadar International Airport	-	230
Necessary facilities of fresh water treatment, water supply and distribution	-	PKR~11bln
300MW Coal-Fired Power Project at Gwadar	-	542
5 MGD Water Desalination Plant Gwadar	-	PKR~5bln

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Local | Supply

- Generally, material cost constitutes a major portion of the cost of sales of the construction companies followed by salaries and wages of both technical staff and labor. The basic construction material like cement and steel is available locally, although raw materials for each have to be procured through imports.
- Although the sector is capital-intensive in nature, labor plays an important role too. The sector employs ~9.5%* of 10 years and above employed persons in the country, whereas ~37.4% are employed in the agriculture segment of the economy.
- Labor wages for the skilled have, on average (FY19-23), been ~55% higher than those for the unskilled. In FY23, the former recorded at PKR~1,711, with YoY increase of ~11.7%, whereas the latter stood at PKR~1,186, up ~14.8% YoY. Meanwhile, inflation was up ~29.1% YoY during the same period.



*Latest available as of FY21.

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Business Cycle



Every construction project has the following 7 stages in its life cycle:

- **Win Contract:** After successful bidding the contract is awarded to the contractor.
- **Mobilization Advance:** Is given to the contractor so that machinery, equipment and labor can be mobilized.
- **Construction Starts:** Within a stipulated time period, as mentioned in the contract.
- **Stages of Completion:** The project is divided into certain number of stages and the contractor is paid after successful completion of each milestone.
- **Delivery:** The project needs to be delivered within an agreed timeframe after which the contractor may accrue damages.
- **Certificate:** When the client is satisfied and there are no pending disputes, a certificate of completion is issued.
- **Retention Money:** Is returned to the contractor after completion of a certain time period after project delivery.

Construction

Business Cycle

Major Delay Causes with Responsible Entities | Delay Categories

Cause of Delay	Category of Delay	Responsible Entity	Delay Criticality Ranking
Change orders/ directives	Contract Related Delays	Owner	1
Labor productivity issues	Labor Related Delays	Contractor	2
Poor site management and supervision	Management/ Administrative Delays	Contractor	3
Inspections/ Audits	Construction Site Related Delays	Contractor	4
Poor cost estimation & control	Management/ Administrative Delays	Contractor	5

- The biggest delay in the construction deadline is caused by the owner. Any changes in design or orders could delay or even halt the construction activity all together.
- Availability of skilled labor is also an issue for the contractor especially in rural areas. The second most deteriorating reason for any project is poor cost estimation and management.

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Business Cycle

Categorical Delay | Criticality Ranking with Responsible Entities

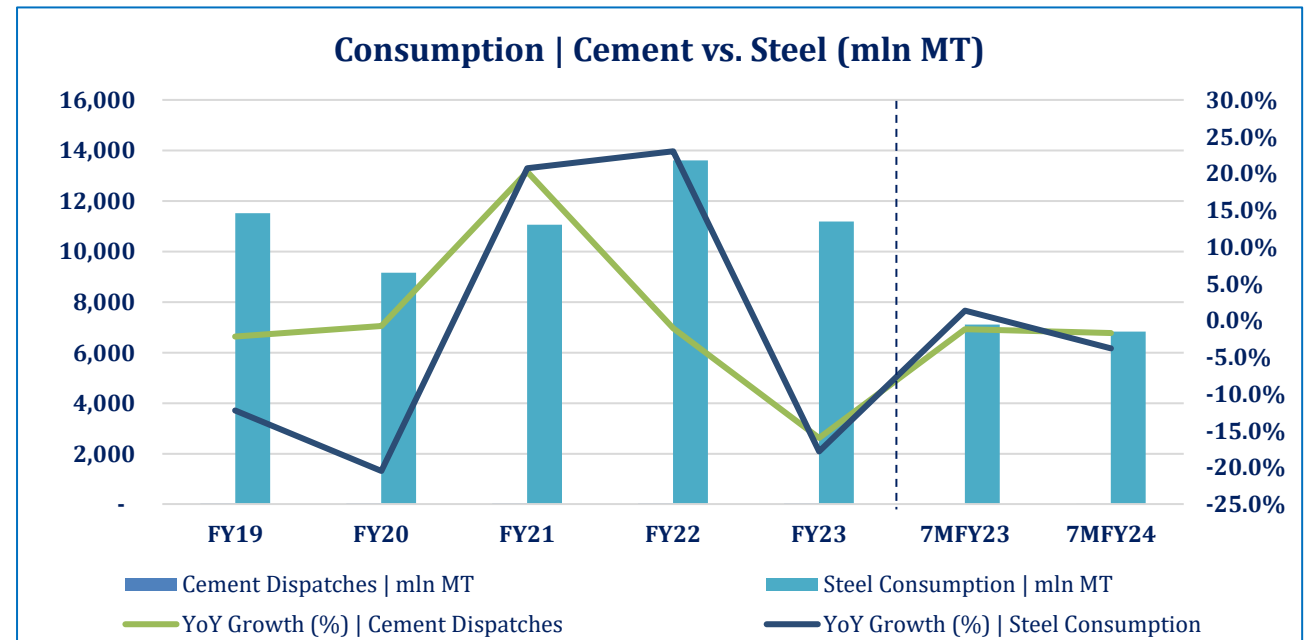
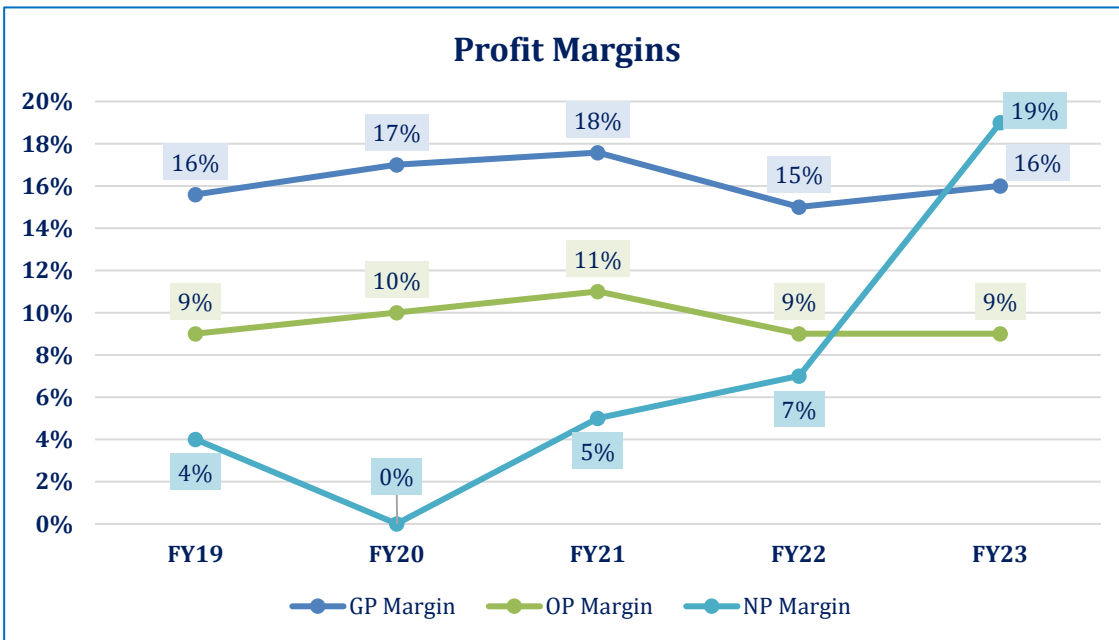
Category of Delay	Major Responsible Entity	Delay Criticality Ranking
Design related delays	Consultant	1
Financial/ economic delays	Owner	2
Contract-related delays	Owner	3
Construction site related delays	Contractor	4
Subcontracted work related delays	Contractor	5

- After design related delays, unavailability of funds is the most crucial element. Subcontracted or third party contractors are also a major element. Their profitability is not directly tied towards the project or contract, hence delays in regarding subcontractors or third party related work are more frequent.
- Although time delay and cost overrun are very common in construction projects but it can be reduced or eliminated by adopting a proper performance monitoring mechanism and control system that will be integrated with all the key aspects and activities of each phase of the construction project.
- Better communication among all the stakeholders of the projects with a clear understanding of the project success criteria and KPI will lead to the successful completion of the project without delay and cost overrun but providing the best quality.

Construction

Local | Business Risk

- The sector's average gross profit margin in FY23 increased to ~16%, with revenue registering ~9.0% uptick against ~28.0% decrease in COGS. Of the total COGS, labor wages held ~19.0% share and grew by ~19.1% YoY, while raw material, holding ~67.2% share, increased by ~24.0% YoY. This likely coincided with ~39.0% PKR depreciation, however, SBP-imposed restrictions likely provided some buffer.
- The sector's operating margin remained steady at ~9.0% whereas, the net margin increased to considerably ~19.0% (FY22: ~7.0%) owing to a ~52.0% lower finance costs due to lower borrowings.
- Hike in material prices are influenced by high energy prices (both cement and steel manufacturing are energy-intensive processes). Massive PKR devaluation (~39.0% YoY) and SBP-imposed import restrictions during May'22-Jun'23 resulted in ~18.0% dip in steel consumption (steel especially is dependent on imported steel scrap), while cement dispatches were also down ~16.0% YoY.

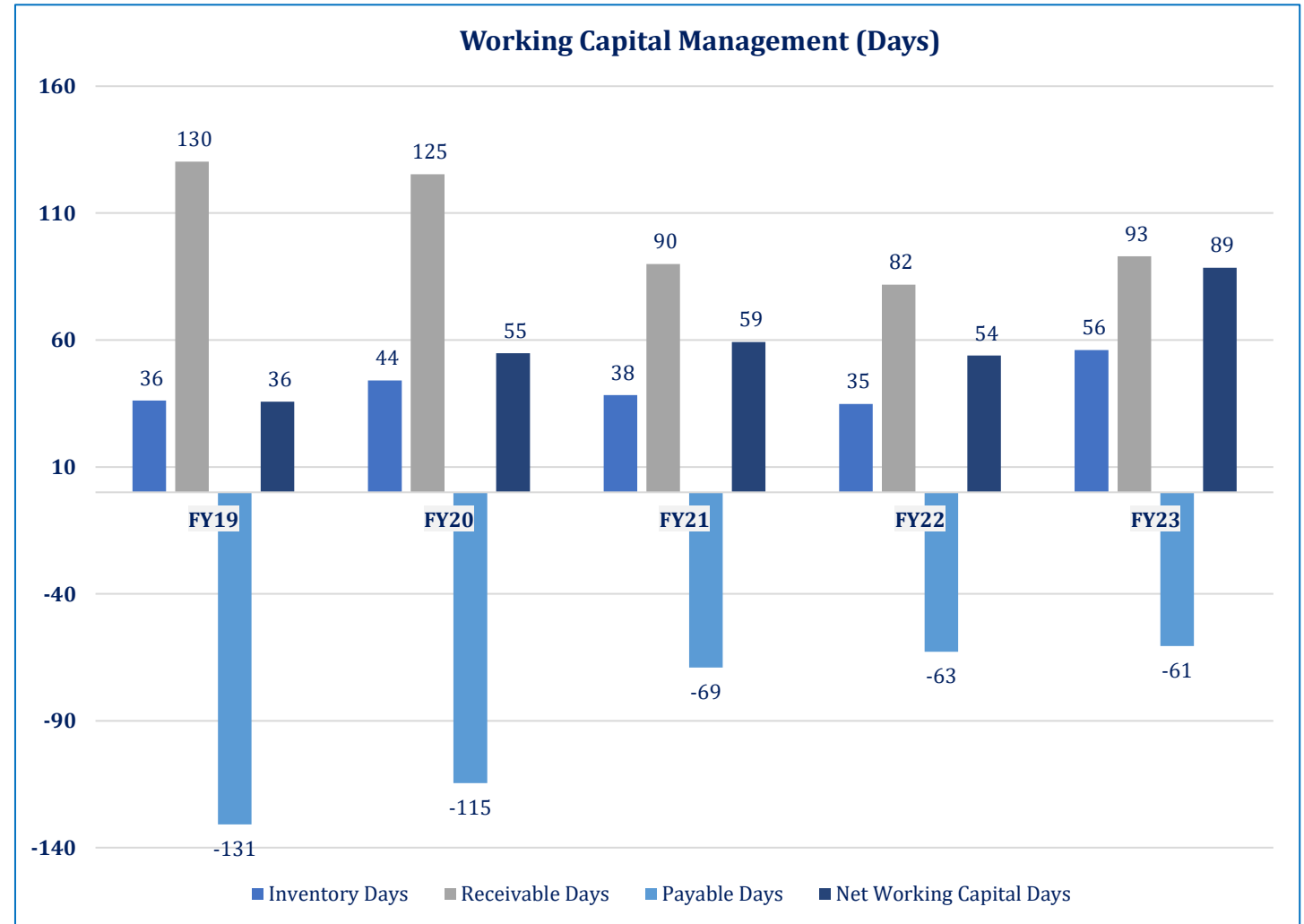


Note: Margins are revenue-weighted and reflective ~8 PACRA-rated/ Listed sector players in FY23.

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Local | Financial Risk

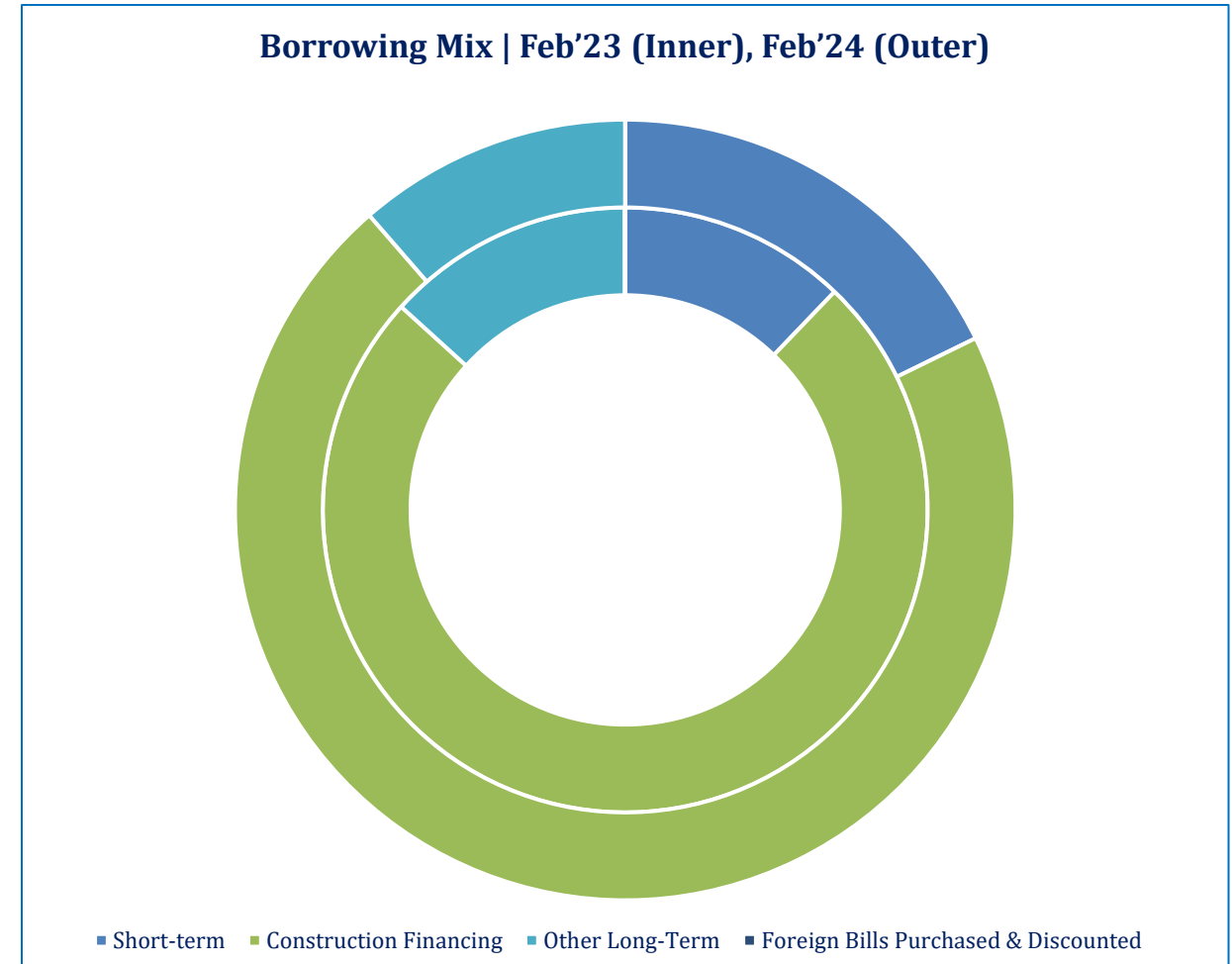
- Construction is a capital-intensive business requiring uninterrupted financial backing from banks. The nature of construction work is uneven wherein delays and prolonged deadlines are often times common. These render construction sector's working capital needs high, reflecting in high dependence on long-term debt.
- In FY23, the sector's average working capital days were recorded at ~89 days (FY22: ~54 days), as inventory days increased to ~56 days (FY22: ~35 days) owing largely to growth in inventories by ~75.0% YoY. This likely was due to an overall slowdown in construction activity during the year.
- Meanwhile, average receivable days also registered an increase of ~11 days and clocked in at ~93 days. However, the sector's payable days declined by just ~2 days to ~61 days in FY23 (FY22: ~63 days), coinciding with lower borrowing during the year.



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Local | Financial Risk

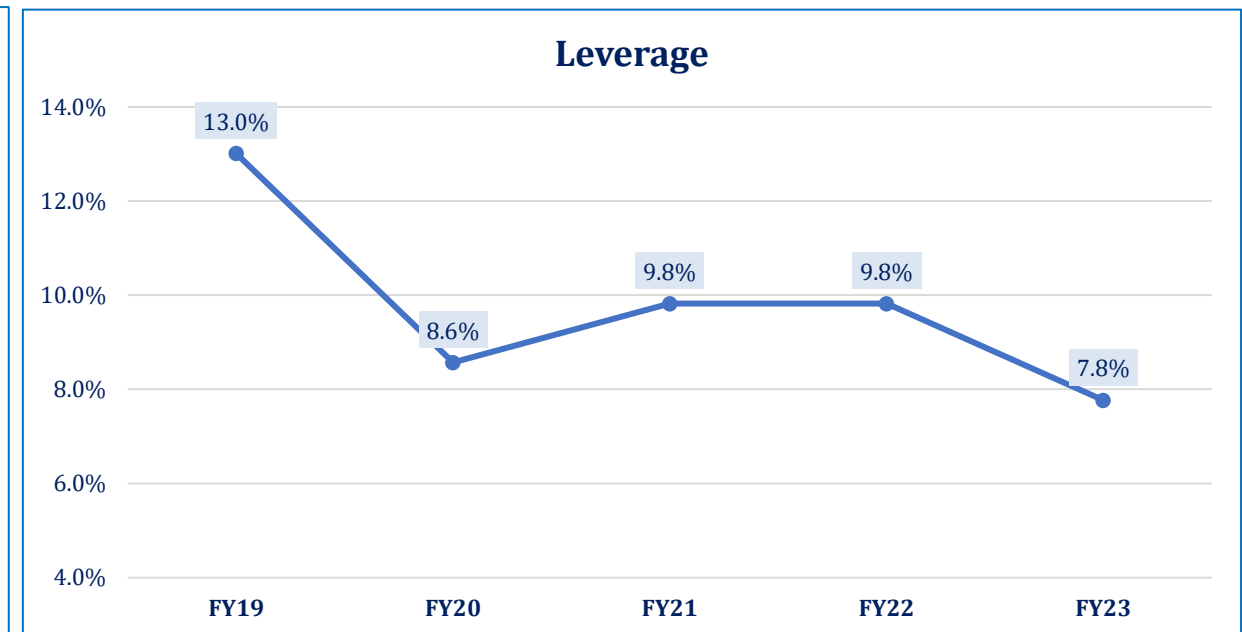
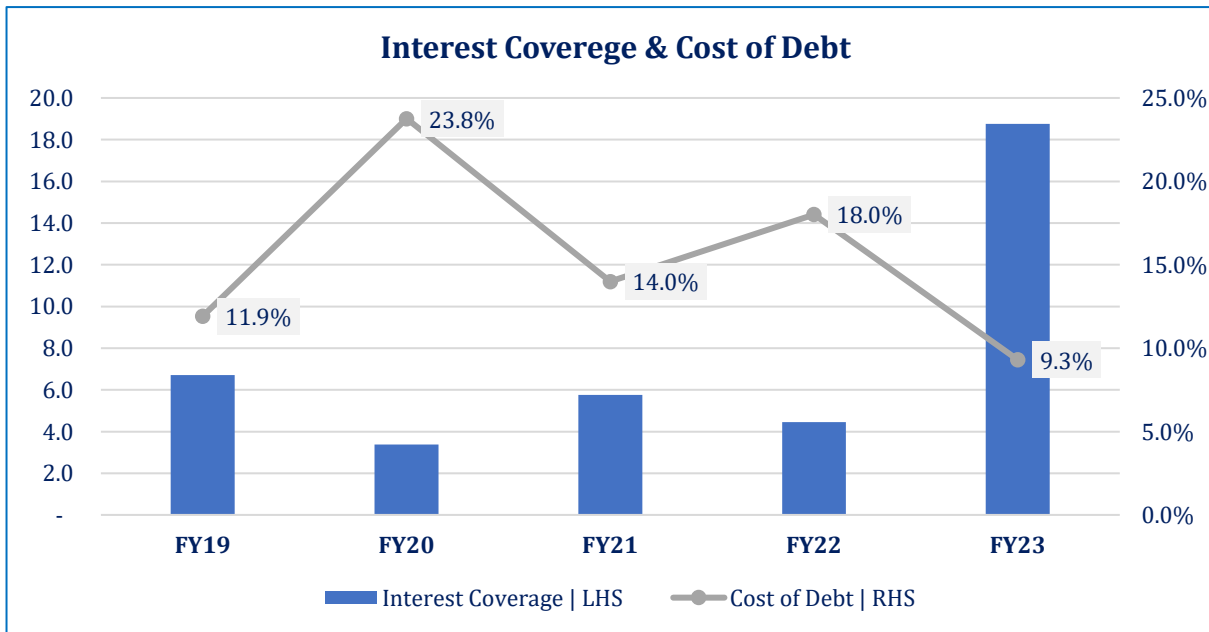
- As of End-Feb'24 the sector's borrowings stood at PKR~198bln, up ~3.0% YoY (End-Feb'23: PKR~193bln).
- Construction financing stood at PKR~141bln down ~2.1% YoY and held the largest share in the sector borrowing mix at ~70.9% (End-Feb'23: ~74.6%).
- While LTFF & TERF as at End-Feb'24 stood at PKR~2.6bln (End-Feb'23: ~2.6bln), up ~0.2% YoY with a share of ~1.3% in the borrowings mix (End-Feb'23: ~1.3%).
- Other long-term financing stood at PKR~22.6bln, down ~11.6% YoY and held a share of ~11.4% in overall borrowings (End-Feb'23: ~13.3%).
- Export and Import financing schemes (both concessional and non concessional) stood at PKR~986mln, holding less than ~1% share in the total borrowings mix.
- Financing from other short-term sources stood at PKR~35bln, up ~50.1% YoY and held a share of ~17.7% in the total borrowings mix (End-Feb'23: ~12.2%).



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Local | Financial Risk

- During FY23, the sector's long-term borrowing was down ~35.0% YoY, while equity increased by ~21.0% YoY resulting in an overall decline in leverage to ~7.8% (FY22: ~9.8%).
- Although, the policy rate was increased from ~13.8% in Jun'22 to ~22.0% in Jun'23, ~6.0% YoY lower total borrowings resulted in average finance cost reducing by ~52.0% YoY. This led to a lower cost of debt at ~9.3% (FY22: ~18.0%). Additionally, the interest coverage ratio of the sector improved to ~18.8x (FY22: ~4.5x).
- The policy rate has been kept steady since Jul'23 at ~22%. Meanwhile, the PKR has appreciated ~2.4% YoY during 8MFY24.

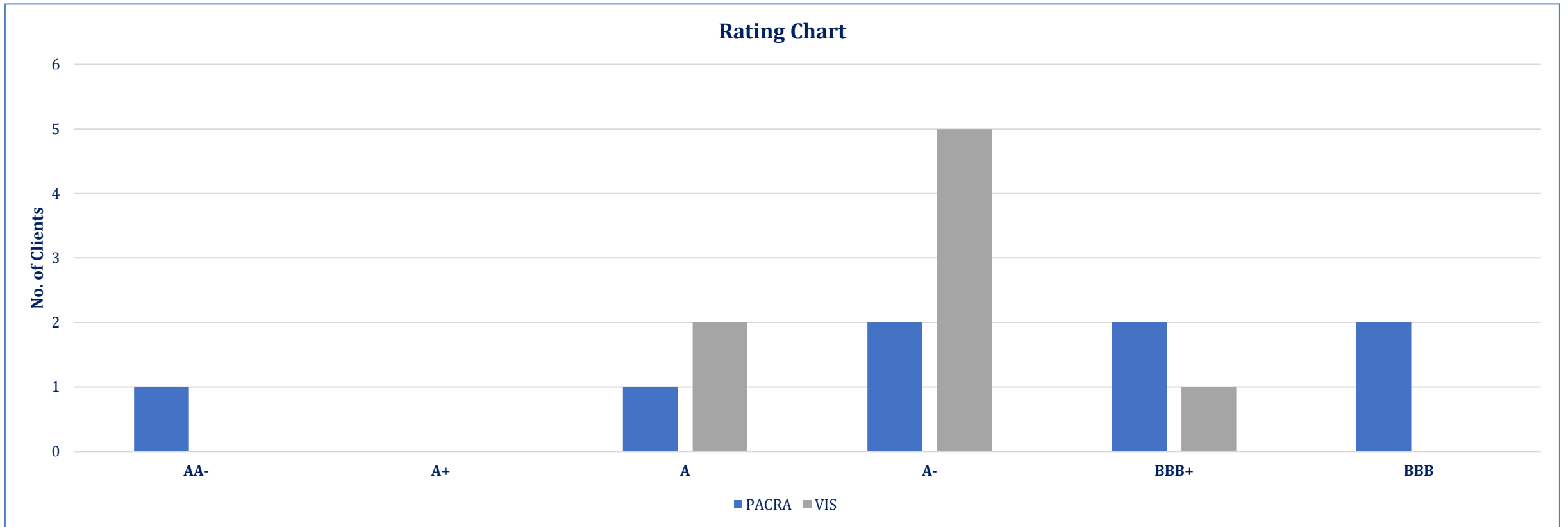


Note: Data is reflective of ~8 PACRA-rated/ Listed sector players in FY23

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Rating Curve

- PACRA rates 8 players of the construction sector with a long-term rating bandwidth ranging from BBB to AA-. No change in rating for 7 players was observed.



Construction

SWOT Analysis

- Considerable labor force
- Government incentives and support
- Readily available raw materials
- Increased government spending

Strengths

Weaknesses

- Unskilled labor.
- Lack of Technology Innovation
- Highly Impacted by Allied Industries
- Deadlines and Delays

- Low barrier to entry
- Exchange rate fluctuation
- High inflation
- Linkages with allied sectors i.e., steel, cement etc.

Threats

Opportunities

- Government initiatives
- Lower Capital Gain Tax
- Advancement in Technology

Construction

Outlook: Stable

- In FY23, Pakistan's economy posted a real GDP contraction of ~0.17% (FY22: ~6.1% growth). Meanwhile, the LSM shrunk by ~10.3% (FY22: ~11.8%), owing majorly to supply-chain disruptions which resulted from SBP-imposed import restrictions, along with the flash floods of Aug'22 and consequent sluggish demand across major industrial sectors of the country. In 2QFY24, however, the real GDP growth stood at ~1.0% (SPLY: ~2.2%).
- Meanwhile, the SBP estimates the GDP growth at ~2-3% for FY24, while IMF reduced Pakistan's GDP forecast to ~2.0%. FY23 was also marred by significantly high levels of inflation with average national CPI recording at ~29.4% (SPLY: 21.3%). However inflation has eased and stood at ~23.1% as at Feb'24 (Feb'23: ~31.5%). Additionally, the PKR experienced depreciation of ~39.0% against the USD during FY23. Meanwhile, the MPR has stood steady at ~22.0% Jun'23.
- The local construction sector is classified as a Large Scale Manufacturing (LSM) industrial component within the industrial sector. The Construction sector is classified under the Industrial Activities segment of the economy. In 2QFY24, the sector experienced a negative growth of ~17.6% (2QFY23: ~-5.0%; 1QFY24: ~0.7%). During FY23, despite the sector recording ~18.4% YoY growth in terms of market size, its share in Industrial activities was down to ~12.5% (SPLY: ~13.6%). This decline was attributed to factors like increases in input prices and wages, higher borrowing cost, and slower growth in development spending.
- Moreover, the floods of Jul-Aug'22, expiry of amnesty schemes, and constraints in fresh disbursements in subsidized lending schemes such as Mera Pakistan Mera Ghar scheme also adversely impacted the sector. PSDP FY24 was up ~30.7% YoY, recording at PKR~950bln. During 7MFY24, PKR~372bln has been authorized, with total expenditure amounting to PKR~161.7bln. Moreover, the Budget FY24 has envisaged, under Current and Development Expenditure on Revenue Account, amounts of PKR~40.5bln and PKR~39.1bln on account of Construction & Transport (SPLY: PKR~30.2bln and PKR~55.2bln, respectively)*.
- During FY23, the sector's long-term borrowing was down ~35.0% YoY, while equity increased by ~21.0% YoY resulting in an overall decline in leverage to ~7.8% (FY22: ~9.8%). Although, the policy rate was increased from ~13.8% in Jun'22 to ~22.0% in Jun'23, ~6.0% YoY lower total borrowings resulted in average finance cost reducing by ~52.0% YoY. This led to a lower cost of debt at ~9.3% (FY22: ~18.0%). Additionally, the interest coverage ratio of the sector improved to ~18.8x (FY22: ~4.5x).
- Going forward, the sector's performance is likely to stay rangebound, given the fact that in 7MFY24 period, production of cement, glass plates and sheets and steel products (including long and flat) registered ~(-0.1)%, ~3.5% and ~0.5% YoY growth, respectively. In 1HFY24, however, construction exhibited ~17.6% YoY decline.

Construction

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