



The Pakistan Credit Rating Agency Limited

Rating Report

EFG Hermes Pakistan Limited

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Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
30-Jun-2018	A-	A1	Stable	Maintain	-
23-Jun-2017	A-	A1	Stable	Initial	-

Rating Rationale and Key Rating Drivers

The entity rating of EFG Hermes Pakistan Limited demonstrates its emerging position in the country's brokerage industry. Strong sponsor support, good governance framework and company's ability to manage risks are the key traits. Company's market share is growing due to strengthening of its customer base. The eight member board of the company includes one independent director. The company has a well-designed organizational structure, with the senior management reporting to the respective heads at group level. Ongoing efforts have been put for full integration of the group's policies at company level.

The research department has foreign alliance and is centralized in U.A.E. As a group policy, the company does not engage in proprietary trading which keeps the market risk low. The company could not reach a break-even point and reported a loss of PKR 6 million for 1QCY18. The company has availed external financing for its margin book. The equity base of PKR 239 million gives modest capacity to absorb the financial risk. Enhancement in retail and foreign sales would further add diversity and support to the brokerage revenues.

Improvement in profitability, continuous monitoring of risk related parameters and retention of key human resource will bode well for the company. The rating requires the company to enhance the diversity and volumes of revenue for establishing a competitive position in the brokerage industry.

Disclosure

Name of Rated Entity	EFG Hermes Pakistan Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology Securities Broker (Mar-17)
Related Research	Sector Study Brokerage / Securities(Oct-17)
Rating Analysts	Shahzaib Khalid shahzaib.khalid@pacra.com +92-42-35869504

EFG HERMES PAKISTAN PROFILE	
Incorporated	1999
Major business lines	<ul style="list-style-type: none"> • Securities Brokerage • Securities Research • Investment Advisory • Forex and Money Market
Legal status	Listed on PSX
Number of branches	2

INDUSTRY SNAPSHOT
<ul style="list-style-type: none"> ▪ Fragmented industry with 305 brokers (SECP list of registered brokers as on Nov 30, 2016). ▪ Total number of registered UINs as on June 30, 2017 – 245,758. ▪ Total number of listed scrips - 529 as on June 30, 2017. ▪ Stringent regulatory framework governed by SECP, PSX, NCCP and CDC.

OWNERSHIP

- **Profile** - EFG Hermes Pakistan Limited is a subsidiary of EFG Hermes Frontier Holdings LLC. The company was incorporated in 1999 as Invest and Finance Securities. In May 2017, after the acquisition by EFG Frontier Holding LLC, company's name changed to EFG Hermes Pakistan Limited.
- **Ownership** - EFG Hermes Frontier Holdings LLC owns 51% of the company, around 29% is owned by a group of five individuals and 20% is free float.

GOVERNANCE

- **Board Structure** - Company's board is composed of eight members including the CEO, Mr. Muzammil Aslam. One board member is independent and seven board members represent EFG Hermes. Mr. Murad Ansari is currently the chairman of the board. He has over 16 years of experience in equity research and sales.
- **Board Committees** - Audit and HR and Remuneration committees exist at board level. The audit committee is chaired by Mr. Murad Ansari, executive director.
- **Board Effectiveness** – Three board meetings were held in the nine months ended March 2018. The board meeting minutes elaborate the quality of discussions held at board level.
- **Financial Transparency** - Company's external auditor, Riaz Ahmad, Saqib, Gohar & Co has expressed an unqualified opinion on the financial statements of 1HFY18.

MANAGEMENT

- **Organizational Structure** - EFGH has a lean organizational structure with experienced and qualified management team with a mix of professionals from finance industry.
- **Members' Profile** - Mr. Muzammil Aslam, CEO carries more than 10 years of experience in the field of economics, capital markets, research and business development.
- **Reporting** - All the departmental heads report directly to the CEO. The compliance head and company secretary, report to the board of directors.

RISK MANAGEMENT

- **Internal Audit** – To ensure effective internal control systems, EFG has placed an independent internal audit function which reports to the audit committee.
- **Compliance** - The Company has a separate risk and compliance function in place which is being headed by Mr. Shahid Kamal. The compliance department ensures effectiveness of all regulatory and internal compliances.
- **Market Risk** - EFGH, as a group policy does not engage in proprietary investments. Therefore, the market risk is low.
- **Credit Risk** – To keep credit risk low, the Company requires its clients to deposit and maintain margin against their outstanding exposures. The risk manual of the group has been finalized and yet to be implemented.

BUSINESS RISK

- The operating revenues were PKR 36 million for 1QCY18 as compared to PKR 30 million for the same period last year. The increase was mainly due to improvement in Company's market share by expanding retail and institutional client base.
- The company was successful in achieving operational breakeven despite the 23% rise in administrative expenses.
- Loss of PKR 6 million was registered in 1QCY18 (PKR 16 million loss in 6MFY18). This was largely due to the higher financial charges of PKR 6 million, which were witnessed on account of higher mark up on finance.
- EFGH has successfully established the investment banking department which would help in diversifying the revenue stream.

FINANCIAL RISK

- The company has an equity base of PKR 239 million which provides cushion against losses.
- Net capital balance was PKR 446 million at 31st December, 2017. This allows EFGH to take exposure up to 25 times (PKR 11.2 billion) which gives EFGH modest capacity to execute trade. During the period, company has paid back the term finance facility by PKR 275 million. Currently, the long term loan facility is PKR 375 million which is obtained by a commercial bank on behalf of EFG Hermes Frontier Holdings LLC.

RESEARCH

- The research function at EFGH is completely integrated at group level. The research function has proper allowance with EFG Frontier Holding LLC.
- The company provides extensive research on public listed companies, macro-economic and market trends.
- The research reports are reviewed by a committee based in Middle East for better quality and service.



BALANCE SHEET	31-Mar-18	30-Jun-17	30-Jun-16	30-Jun-15
	1QCY18	FY17	FY16	FY15
	Unaudited	Audited	Audited	Audited
EARNING ASSETS				
Finances	118	76	0	0
Investments	325	613	84	435
	443	688	84	435
NON-EARNING ASSETS				
Cash and Bank Balances	148	99	48	130
Trade debts	42	86	33	17
Advances, Deposits and Other receivables	80	144	34	65
Others (including Fixed Assets)	99	91	77	50
TOTAL ASSETS	812	1,109	276	696
Equity	239	256	192	457
Borrowings	382	720	7	0
Other Liabilities (Non-Interest Bearing)				
Trade Creditors	120	90	49	414
Other Liabilities	71	44	28	27
TOTAL EQUITY & LIABILITIES	812	1,109	276	898
INCOME STATEMENT	31-Mar-18	30-Jun-17	30-Jun-16	30-Jun-15
	1QCY18	FY17	FY16	FY15
	<i>Unaudited</i>	<i>Audited</i>	<i>Audited</i>	<i>Audited</i>
Fee-Based Income				
Fees	0	0	1	0
Commission	0	0	0	0
Brokerage	35	124	75	86
Others	0	0	0	2
Operating Expenses	(38)	(129)	(89)	(72)
Fee Based Income / (Loss)	(2)	(6)	(13)	16
Non Fee-Based Income	3	59	7	95
Total Operating Income / (Loss)	1	53	(6)	111
Financial Charges	(6)	(9)	(1)	(5)
Other Income / (Loss)	4	2	1	44
Profit / (Loss) Before Tax	(1)	45	(6)	150
RATIO ANALYSIS	31-Mar-18	30-Jun-17	30-Jun-16	30-Jun-15
	1QCY18	FY17	FY16	FY15
	<i>Unaudited</i>	<i>Audited</i>	<i>Audited</i>	<i>Audited</i>
Performance				
Net Profit Margin	(17%)	30%	(13%)	157%
Cost-to-Fee Income	107%	105%	118%	82%
Working Capital				
Overdue Accounts Receivable / Total Accounts Receivable	0%	7%	9%	1%
Overdue Accounts Receivable / (Short Term Borrowings + Accounts Payable)	0%	10%	87%	0%
Accounts Receivable / (Short Term Borrowings + Customer Advances + Accou	22%	44%	42%	50%
Exposure				
Investments / Equity	153%	268%	44%	95%
Liquidity				
Trade Related Assets / Trade Related Liabilities	35%	96%	67%	53%
Liquid Assets / (Short term Borrowings + Advances from Customers + Accoun	343%	429%	175%	126%
Liquid Investments / Equity	130%	246%	22%	86%
Coverages				
EBITDA/Gross Interest	1	6	(1)	24
FCFO/Gross Interest	0	4	(11)	21
FCFO/Gross Interest+CMLTD+Uncovered Short Term Borrowings	(1)	(6)	1	(24)
Total Debt (excluding Covered Short Term Borrowings) / FCFO	221	19	(1)	0
Capital Adequacy				
Equity / Total Assets	26%	21%	70%	51%
Total Debt / Equity	159%	281%	4%	0%



ENTITY CREDIT RATING SCALE & DEFINITIONS

Credit rating reflects forward-looking opinion on credit worthiness of underlying entity; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.			
LONG TERM RATINGS		SHORT TERM RATINGS	
AAA	Highest credit quality. Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments.	<p>A1+: The highest capacity for timely repayment.</p> <p>A1: A strong capacity for timely repayment.</p> <p>A2: A satisfactory capacity for timely repayment. This may be susceptible to adverse changes in business, economic, or financial conditions.</p> <p>A3: An adequate capacity for timely repayment. Such capacity is susceptible to adverse changes in business, economic, or financial conditions.</p> <p>B: The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions.</p> <p>C: An inadequate capacity to ensure timely repayment.</p>	
AA+	Very high credit quality. Very low expectation of credit risk. Indicate very strong capacity for timely payment of financial commitments. This capacity is not significantly vulnerable to foreseeable events.		
AA			
AA-			
A+	High credit quality. Low expectation of credit risk. The capacity for timely payment of financial commitments is considered strong. This capacity may, nevertheless, be vulnerable to changes in circumstances or in economic conditions.		
A			
A-			
BBB+	Good credit quality. Currently a low expectation of credit risk. The capacity for timely payment of financial commitments is considered adequate, but adverse changes in circumstances or economic conditions are more likely to impair this capacity.		
BBB			
BBB-			
BB+	Moderate risk. Possibility of credit risk developing. There is a possibility of credit risk developing, particularly as a result of adverse economic or business changes over time; however, business or financial alternatives may be available to allow financial commitments to be met.		
BB			
BB-			
B+	High credit risk. A limited margin of safety remains against credit risk. Financial commitments are currently being met; however, capacity for continued payment is contingent upon a sustained, favorable business, and economic environment.		
B			
B-			
CCC	Very high credit risk. "CCC" Default is a real possibility. Capacity for meeting financial commitments is solely reliant upon sustained, favorable business or economic developments. "CC" Rating indicates that default of some kind appears probable. "C" Ratings signal imminent default.		
CC			
C			
D	Obligations are currently in default.		
Rating Watch	Outlook (Stable, Positive, Negative, Developing)	Suspension	Withdrawn
Alerts to the possibility of a rating change subsequent to, or in anticipation of, a) some material identifiable event and/or b) deviation from expected trend. But it does not mean that a rating change is inevitable. Rating Watch may carry designation – Positive (rating may be raised, negative (lowered), or developing (direction is unclear). A watch should be resolved within foreseeable future, but may continue if underlying circumstances are not settled.	Indicates the potential and direction of a rating over the intermediate term in response to trends in economic and/or fundamental business or 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'.	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, a suspended rating should be considered withdrawn.	A rating is withdrawn on a) termination of rating mandate, b) cessation of underlying entity, c) the debt instrument is redeemed, d) the rating remains suspended for six months, or e) the entity/issuer defaults.
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Rating Team Statements

(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

Restrictions

- (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.
- (8) PACRA prohibits its employees and analysts from soliciting money, gifts or favors from anyone with whom PACRA conducts business | Chapter III; 11-A-(q)
- (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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