



The Pakistan Credit Rating Agency Limited

Rating Report

Etimaad Engineering (Pvt.) Limited

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Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
16-May-2019	BBB-	A3	Stable	Maintain	-
28-Dec-2018	BBB-	A3	Stable	Maintain	-
30-Jun-2018	BBB-	A3	Stable	Upgrade	-
10-Jan-2018	BB+	A3	Stable	Maintain	-
13-Jun-2017	BB+	A3	Stable	Maintain	-

Rating Rationale and Key Rating Drivers

The ratings demonstrate Etimaad's strength which stimulates from its sustained operational history. The business has optimal mix of contracts in its domain and has managed to complete reasonable number of contracts in Pakistan. The slowdown in revenue for the current period has been primarily due to delay on some sizable projects. The pipeline is healthy; therein for the sake of sustainable long term growth, management follows a balanced approach aiming to gain more share in different lines of businesses. The entity is following a pyramid strategy; the top being mega projects (EPC), followed by construction and lastly maintenance related projects. The entity is eyeing further diversity in its revenue stream in the near future from specific dimension of real estate development project. Management efforts to recover previous years losses is expected to materialize by end-FY19. Company is adequately leveraged and determined to reduce its conventional borrowing over a short term horizon. The performance of the company rests with projects in hand and timely completion. The sponsors have demonstrated their commitment by operationally supporting the business by providing security and personal guarantees to obtain financial facilities. Meanwhile, strengthening of business development structure by inducting expert and experienced professionals is considered a key catalyst for upcoming projects.

Rating is dependent upon several contracts successfully completed and upcoming projects undertaken by management to streamline its business for improved profitability, which is pivotal for considerable growth.

Disclosure

Name of Rated Entity	Etimaad Engineering (Pvt.) Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology Corporate Ratings(Jun-18),Methodology Criteria Rating Modifier(Jun-18),Methodology Correlation Between Long-Term And Short-Term Rating Scale(Jun-18)
Related Research	Sector Study Construction(Mar-19)
Rating Analysts	Muhammad Noor ul Haq muhammad.noorulhaq@pacra.com +92-42-35869504

Profile

Legal Structure Etimaad Engineering Private Limited (Etimaad), was incorporated in Pakistan under the repealed Companies Ordinance, 1984 as a private limited company on May 11, 2007.

Background Etimaad was established by a team of professionals from Descon Engineering Limited who are also the shareholders of the company. Over the years, the sponsors have established similar businesses mainly in Saudi Arabia (subsidiary) and Qatar (associate). In 2014, Etimaad had to divest its share in Arabian Etimaad Industrial Company, for an amount of SAR 5mln (PKR 133mln), due to geopolitical tensions at Yemen border and turmoil in oil prices. The company has completed various projects in Pakistan and overseas.

Operations The company is principally engaged in engineering, procurement, manufacturing, construction and project management activities.

Ownership

Ownership Structure Mr. Mazharuddin Ansari's family directly own 37.4%, Mr. Farooq Hussain Mughal 26.9%, Mr. Mohammad Sohail Shafique 25.6% and others 10.1% stake in Etimaad.

Stability The experienced professionals of the company providing expertise and exposure to operate efficiently as one of the leading company in Pakistan.

Business Acumen The sponsors have rich industry experience and are considered as leaders in the engineering industry.

Financial Strength The sponsors have an adequate financial profile. Although there is no explicit commitment, but key sponsor's support to Etimaad is demonstrated as they have provided personal guarantees to secure loans and guarantees from FIs.

Governance

Board Structure The company's board comprises two members including the Chairman – Mr. Mohammad Sohail Shafique, and President & CEO – Mr. Farooq Hussain Mughal.

Members' Profile Mr. Mohammad Sohail Shafique, the Chairman, has more than two decades of experience in renowned organizations. He is an Engineer by profession and alumni of UET Lahore.

Board Effectiveness Both of the board members carry executive roles in the management of the company. To provide desired challenge to the management's decisions and strengthen overall governance framework, representation of independent director is important.

Financial Transparency Grant Thortan Anjum Rehman, Chartered Accountants, is the external auditor of the company. The auditor gave an unqualified opinion on the company's financial statements for the year ended June 30, 2018.

Management

Organizational Structure There are a large number of reporting lines reporting in to CEO. Although this may limit strategic focus, support from senior executive members and Chairman, provides comfort.

Management Team Mr. Farooq Hussain Mughal, the President & CEO, is finance professional and associated with Etimaad since its inception. Previously he worked as CFOO in Etimaad before he elevated to the position of President & CEO in FY15. He is supported by an able and competent team of professionals.

Effectiveness Majority of senior management has long ties with Descon Engineering Limited in the past. Project related hiring occurs as per the project's need; therefore ETIMAAD tries to recruit suitable technicians and proletariat. In a bid to strengthen the business development part of the business, a new addition to the team, Syed Abrar Ali Khan is the Vice President of Etimaad. Previously he served as GM Descon-UAE Business Area.

MIS The company has an integrated financial, cost control and project management system to smooth sail the business processes from initiation to close and feedback phases. The ERP system includes modules on (i) ETest – Bid preparation, (ii) Primavera P6- Scheduling, monitoring the project and generation of reports, (iii) Tanseeb – Mtrix software linked to ETest to execute project activities and monitors the actual progress, (iv) ETFin- Financial management system integrated with ETest and Primavera, (v) EOffice - facilitates company-wide information sharing.

Control Environment The EPC industry is always prone to Quality, Health, Safety and Environmental (QHSE) issues. Therefore, Etimaad complies with applicable laws and relevant industry standards.

Business Risk

Industry Dynamics Construction sector's share in GDP in FY18 was 2.82% against a share of 2.74% last year. This sector has witnessed a growth of ~9% against a growth of ~10% last year, as many CPEC related projects were ongoing during 2016-17. During FY18 Federal PSDP utilization out of PKR ~1 tln was almost PKR ~750 bln, whereas Provincial ADP utilization out of PKR ~1.12 tln was PKR ~800 bln. For FY19 the Federal Government has allocated PKR ~800 bln under PSDP spending, and considering 70% utilization history, there is a major cut in the expected construction activity which doesn't bode very well for the economy. Although if / when PMs' ambitious plan to build 5 million houses goes through it would provide a major impetus to the debilitating construction industry.

Relative Position Etimaad is eyeing for optimal growth both in terms of turnover and profitability through a better mix of construction and maintenance projects. Company now takes appropriate measures to avoid any discrepancy in the projects while ensuring timely completion of the project.

Revenues During FY18, topline of Etimaad witnessed a growth of ~24% on YoY basis (FY17: 3.2%; FY16: 39.5%) while the revenue for 9MFY19 decreased by 7.5% (9MFY18: 27.6%). Overall mix of in-hand projects comprises recurring business (53%) and new project-based business (47%).

Margins Since FY11, loss making projects have strained company's profits. Thus, the company continued to absorb earlier year's losses. The company operates on thin margins. During FY18, gross margins remained stagnant on YoY basis (FY18: 21.8%; FY17: 18.3%; FY16: 18.4%). Controlled finance cost (PKR 33mln) and slight support from capital gains PKR -2mln (FY17: 2mln; FY16: PKR -2mln); Hence, the company's net profit increased to PKR 74mln (FY17: 34mln; FY16: PKR 20mln). In 9MFY19, attributed to decreased revenues and somehow controlled operating expenses translated in to a bottom line of PKR 30mln (9MFY18: PKR 20mln).

Sustainability Etimaad's management envisage sustainable footing in the market by planning to move to capital market instead of money market for financing needs in near future. Arrangements like; (i) Pak Japan Traders, (ii) LPG storage bullet with Engro Vopak and other projects under negotiations are likely to materialize.

Financial Risk

Working Capital Etimaad's working capital is mainly supported by short term borrowings and internal cash. During FY18, ETIMAAD's net working capital cycle days decreased to 179 (FY17: 224days; FY16: 194days) owing to higher inventory levels still, however, for the period 9MFY19, net working capital days locked at 241days (9MFY18: 237 days; 9MFY17: 260days). To fulfill the needs of working capital, company has availed short term borrowings from various financial institutions worth PKR 210mln in 9MFY19 (9MFY18: PKR 273mln; 9MFY17: PKR 189mln).

Coverages Operating cash flows (FCFO) - denotes performance stability (FY18: PKR 159mln; FY17: PKR 83mln). As for 9MFY19, FCFO decreased to PKR 95mln. Hence translating negatively in Coverage's 9MFY19 3.3% which was previously high in FY18: 4.8%.

Capitalization Etimaad has adequately managed its leveraged capital structure. Debt to debt plus equity ratio was at 42.2% at end-Mar19, (end-Mar18: 46.4%; end-Mar17: 43.5%). However, due to limited cash flows, the loans are jointly secured by sponsors' guarantees.



Etimaad Engineering (Private) Limited

BALANCE SHEET	31-Mar-19	30-Jun-18	31-Mar-18	30-Jun-17	30-Jun-16
	9MFY19	FY18	9MFY18	FY17	FY16
Non-Current Assets	413	421	345	309	178
Investments (Incl. associates)	23	23	3	3	3
Equity	23	23	3	3	3
Debt	-	-	-	-	-
Current Assets	1,252	1,242	1,219	1,029	1,029
Inventory	534	493	499	524	402
Trade Receivables	511	537	414	318	377
Others	208	212	306	187	251
Total Assets	1,688	1,686	1,567	1,340	1,210
Debt	399	415	392	355	255
Short-term	211	310	273	201	155
Long-term (Incl. Current Maturity of long-term debt)	188	106	119	154	100
Other shortterm liabilities	660	661	624	454	511
Other Longterm Liabilities	11	11	7	7	6
Shareholder's Equity	618	599	543	524	438
Total Liabilities & Equity	1,688	1,686	1,567	1,340	1,210

INCOME STATEMENT

Turnover	650	1,150	703	926	897
Gross Profit	139	251	142	169	165
Other Income	2	(2)	0	2	(2)
Financial Charges	(29)	(33)	(28)	(26)	(26)
Net Income	30	74	20	34	20

Cashflow Statement

Free Cashflow from Operations (FCFO)	95	159	64	83	70
Net Cash changes in Working Capital	(42)	3	(42)	(60)	(90)
Net Cash from Operating Activities	24	130	(3)	(1)	(47)
Net Cash from Investing Activities	(31)	(132)	(60)	(100)	(22)
Net Cash from Financing Activities	(27)	13	34	97	23

Ratio Analysis

Performance					
Turnover Growth	-7.5%	24.2%	27.6%	3.2%	39.5%
Gross Margin	21.3%	21.8%	20.1%	18.3%	18.4%
Net Margin	4.6%	6.5%	2.9%	3.7%	2.3%
ROE	6.5%	12.4%	5.0%	6.5%	4.7%
Coverages					
Interest Coverage (FCFO/Gross Interest)	0.1	4.8	2.3	3.1	2.7
Core: (FCFO/Gross Interest+CMLTD+Uncovered Total STB)	0.4	2.2	1.1	1.2	1.3
Total: (TCF) / (Gross Interest+CMLTD+Uncovered Total STB)	0.3	2.2	1.1	1.2	1.3
Debt Payback (Total LT Debt Including UnCovered Total STBs) /	0.3	0.8	3.4	2.8	2.4
Liquidity					
Net Cash Cycle (Inventory Days + Receivable Days - Payable Day)	241.1	179.3	236.7	224.0	193.7
Capital Structure (Total Debt/Total Debt+Equity)	42.4%	44.7%	46.4%	45.0%	42.5%

Credit Rating Scale & Definitions

Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; 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	A1+	The highest capacity for timely repayment.
AA+ AA 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.	A1	A strong capacity for timely repayment.
A+ A 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.	A2	A satisfactory capacity for timely repayment. This may be susceptible to adverse changes in business, economic, or financial conditions.
BBB+ BBB 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 and in economic conditions are more likely to impair this capacity.	A3	An adequate capacity for timely repayment. Such capacity is susceptible to adverse changes in business, economic, or financial conditions.
BB+ BB 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.	B	The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions.
B+ B 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.	C	An inadequate capacity to ensure timely repayment.
CCC CC C	Very high credit risk. Substantial 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.		
D	Obligations are currently in default.		



Outlook (Stable, Positive, Negative, Developing) Indicates the potential and direction of a rating over the intermediate term in response to trends in economic and/or fundamental business/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'.

Rating Watch 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. A watch should be resolved within foreseeable future, but may continue if underlying circumstances are not settled. Rating Watch may accompany Outlook of the respective opinion.

Suspension 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, the rating should be considered withdrawn.

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, e) the entity/issuer defaults, or/and f) PACRA finds it impractical to surveil the opinion due to lack of requisite information.

Harmonization A change in rating due to revision in applicable methodology or underlying scale.

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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

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- (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)
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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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