



The Pakistan Credit Rating Agency Limited

Rating Report

Etimaad Engineering (Pvt.) Limited

Report Contents

1. Rating Analysis
2. Financial Information
3. Rating Scale
4. Regulatory and Supplementary Disclosure

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
03-Mar-2020	BBB	A2	Stable	Upgrade	-
15-Nov-2019	BBB-	A3	Stable	Maintain	-
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	-
13-Jun-2016	BB+	A3	Stable	Initial	-

Rating Rationale and Key Rating Drivers

The ratings demonstrate Etimaad's strength which emanates from its sustained operational history. The upgrade reflects Etimaad's sustained improvement in business performance, with growth in revenue and margin, aided by healthy relationships with existing customers, and extensive experience of the management. 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 customer list portrays some of the best names in the domestic market. The Company has a track record of over a decade with strong capabilities in executing turnkey projects, as reflected in repeat orders from customers. The Company is adequately leveraged and 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. Financial risk metrics need to be upheld.

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-19),Methodology Correlation Between Long-Term And Short-Term Rating Scale(Jun-19),Criteria Rating Modifier(Jun-19)
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 as a private limited company on May 11, 2007.

Background Etimaad was established by a team of professionals with engineering and contracting background having rich industry experience with renowned local and international business houses. They 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 situation and turmoil in oil & gas sector. The Company has successfully completed various projects in Pakistan and overseas.

Operations Etimaad is principally engaged in turnkey/EPC, manufacturing, industrial construction, operation & maintenance and infrastructure development projects.

Ownership

Ownership Structure Mr. Mazharuddin Ansari's family directly owns 37.4%, Mr. Farooq Hussain Mughal 26.9%, Mr. Mohammad Sohail Shafique 25.6%, Mr. Laeeq Uddin Ansari 5.2%, Syed M Najeeb A. Jaffery 3.5% and Mr. Ghulam Kafeel Majal 1.3% stake in Etimaad.

Stability The experienced management team of the Company is providing expertise and exposure to manage the business affairs efficiently enabling to remain as one of the reliable engineering and contracting company in Pakistan.

Business Acumen The sponsors of the Company have rich industry experience and have worthy knowledge of various aspects of the macro and micro economic developments, are keeping abreast of technological advancements and skilled in risk assessment and mitigation through adopting flexibility and adaptability approach in engineering and contracting business.

Financial Strength The sponsors have an adequate financial profile and support to Etimaad is demonstrated as they have provided personal guarantees to secure loans and guarantees from FIs.

Governance

Board Structure Etimaad'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 three decades of experience at leading positions in renowned organizations in Pakistan and overseas. He is an Engineer by profession and alumni of UET Lahore. Mr. Shafique plays an active role in all strategic decisions of Etimaad including long term partnerships, technology collaborations, overseas expansion, local and international networking.

Board Effectiveness The Company being a private company does not comply with the code of corporate governance. Both of the board members carry executive roles in the management of the Company. To provide the desired challenge to the management's decisions and strengthen the overall governance framework, the representation of an independent director on the board is important.

Financial Transparency Grant Thornton 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, 2019.

Management

Organizational Structure Etimaad is working through a typical organization structure where all direct and indirect functions report to the incumbent CEO whereas the CEO report to the Chairman.

Management Team Mr. Farooq Hussain Mughal, the President & CEO, is finance professional and associated with Etimaad since its inception. He is supported by an experienced and competent team of professionals. All members of the senior management team have an average experience of more than 35 years working at leading positions with various local and international companies and are recognized across the industry.

Effectiveness Team Etimaad has been successful in the acquisition and execution of hundreds of projects for blue-chip clients in Pakistan and overseas establishing the effective role as a management team.

MIS Etimaad has integrated financial, cost control and project management systems to efficiently carry out the business processes while implementing SOPs' and controls to ensure the timely and within budget completion of the projects. ERP system has the capability of remote and online connectivity to integrate the projects' data at central location to enable project management and control function for feedback and timely decision making. The ERP system includes various modules such as (i) ETest, (ii) Primavera P6, (iii) Tanseeb, (iv) EFin and (v) EOffice.

Control Environment The EPC and construction projects require the implementation of high standard of Quality, Health, Safety and Environmental (QHSE). Etimaad complies with applicable laws and relevant industry standards. Etimaad is certified with applicable standards from ISO 9001, ISO 14001 and OSHAS18000.

Business Risk

Industry Dynamics The construction & engineering sector comprises construction of bridges, dams, roads and urban infrastructure development which also forms the base and supporting factor for other services sectors. Mostly CPEC related projects remained slow and there was a muted growth during the period under review. For FY19 the Federal Government has allocated PKR ~800bln 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 sector. 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's target market comprises of projects related to thermal and renewable power, fertilizer, oil & gas, chemical and petrochemical, cement, steel and other large-scale industrial units. Etimaad continues its focused approach through generating business from the private sector and multinational corporations. In this domain, Etimaad is a preferred contractor for executing projects involving civil, mechanical, electrical & instrumentation works, O&M, shutdown and retrofit services.

Revenues During FY19, the revenue of the Company deteriorated owing to prevailing uncertain conditions in the engineering sector in the current environment and liquidity crunch due to a lack of investor's confidence. However, the topline witnessed a significant increase of 21.7% as at end-Dec19 (end-Dec18: 1.8%). This growth in revenue is attributed to the new projects awarded and executed during said period. This shows the strength of Etimaad that despite adverse business and economic indicators, the Company has managed to acquire new business and continued with the targeted growth pattern.

Margins Given the challenging economic environment and highly competitive nature of the industry, Etimaad was largely able to maintain gross margin at 22.8% as at end-Dec19 (end-Dec18: 22.3%) due to higher revenue contribution. Despite a significant increase of 66.7% in finance cost, Etimaad also managed its net profit margin at 4.2% (1HFY19: 4.5%). In 1HFY20, somehow controlled operating expenses translated into a bottom line of PKR 23mln (1HFY19: PKR 20mln).

Sustainability Etimaad's management envisages long term sustainable outlook in the market by planning to move to capital market instead of the money market to meet upcoming financing needs. The healthy backlog business ensures sustainable and long term growth and the management continues to follow a balanced business mix approach aiming to gain more share in different lines of businesses. .

Financial Risk

Working Capital The working capital of the Company is mainly supported by short term borrowings and internal cash. During 1HFY20, Etimaad's net working capital days stood at 187(1HFY19: 259days) owing to higher inventory levels and trade receivables. To fulfill the needs of working capital, the company has availed short term borrowings from various financial institutions worth PKR 144mln in 1HFY20 (1HFY19: PKR 299mln). However, the short term trade leverage showed an increasing trend (1HFY20: 43.8%; 1HFY19: 34.4%).

Coverages During 1HFY20, Etimaad's free cash flow (FCFO) denotes performance stability, stood at ~PKR 69mln (1HFY19: PKR 63mln). While debt-servicing coverage also decreased to 3.8x (1HFY19: 5.3x), core debt coverage also in line and deteriorated to 1.1x (1HFY19: 1.5x) due to the interest expense on account of rapidly increased KIBOR leading to the increased cost of borrowings.

Capitalization Etimaad has adequately managed its leveraged capital structure. Debt to debt plus equity ratio was at 41.7% at end-Dec19, (end-Dec18: 46.1). However, to meet cash flow requirements, the funded facilities are jointly secured by sponsors' personal guarantees.



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Financial Summary

PKR mln

Etimaad Engineering (Pvt.) Limited Construction	Dec-19 6M	Jun-19 12M	Jun-18 12M	Jun-17 12M
A BALANCE SHEET				
1 Non-Current Assets	382	409	421	309
2 Investments	-	-	20	-
3 Related Party Exposure	3	3	3	3
4 Current Assets	1,270	1,126	1,242	1,029
<i>a Inventories</i>	513	497	493	524
<i>b Trade Receivables</i>	304	249	343	114
5 Total Assets	1,655	1,538	1,686	1,340
6 Current Liabilities	584	490	664	453
<i>a Trade Payables</i>	214	229	251	144
7 Borrowings	415	405	409	350
8 Related Party Exposure	1	1	3	6
9 Non-Current Liabilities	13	13	11	7
10 Net Assets	642	629	599	524
11 Shareholders' Equity	642	629	599	524
B INCOME STATEMENT				
1 Sales	545	912	1,150	926
<i>a Cost of Good Sold</i>	(421)	(704)	(899)	(757)
2 Gross Profit	124	208	251	169
<i>a Operating Expenses</i>	(39)	(58)	(57)	(47)
3 Operating Profit	85	150	194	122
<i>a Non Operating Income or (Expense)</i>	0	1	(2)	2
4 Profit or (Loss) before Interest and Tax	85	151	192	124
<i>a Total Finance Cost</i>	(31)	(43)	(33)	(26)
<i>b Taxation</i>	(31)	(66)	(84)	(64)
6 Net Income Or (Loss)	23	42	74	34
C CASH FLOW STATEMENT				
<i>a Free Cash Flows from Operations (FCFO)</i>	69	132	159	83
<i>b Net Cash from Operating Activities before Working Capital Changes</i>	36	88	127	59
<i>c Changes in Working Capital</i>	(43)	(60)	3	(60)
1 Net Cash provided by Operating Activities	(8)	28	130	(1)
2 Net Cash (Used in) or Available From Investing Activities	0	6	(132)	(100)
3 Net Cash (Used in) or Available From Financing Activities	3	(42)	13	97
4 Net Cash generated or (Used) during the period	(4)	(9)	11	(4)
D RATIO ANALYSIS				
1 Performance				
<i>a Sales Growth (for the period)</i>	19.4%	-20.7%	24.2%	3.2%
<i>b Gross Profit Margin</i>	22.8%	22.8%	21.8%	18.3%
<i>c Net Profit Margin</i>	4.2%	4.6%	6.5%	3.7%
<i>d Cash Conversion Efficiency (EBITDA/Sales)</i>	20.6%	22.6%	20.6%	16.1%
<i>e Return on Equity (ROE)</i>	7.2%	6.8%	13.3%	7.0%
2 Working Capital Management				
<i>a Gross Working Capital (Average Days)</i>	262	316	234	237
<i>b Net Working Capital (Average Days)</i>	187	220	171	185
<i>c Current Ratio (Total Current Assets/Total Current Liabilities)</i>	2.2	2.3	1.9	2.3
3 Coverages				
<i>a EBITDA / Finance Cost</i>	3.8	5.0	7.7	9.0
<i>b FCFO / Finance Cost+CMLTB+Excess STB</i>	1.1	1.5	2.5	1.5
<i>c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)</i>	3.4	1.9	0.8	2.3
4 Capital Structure (Total Debt/Total Debt+Equity)				
<i>a Total Borrowings / Total Borrowings+Equity</i>	39.3%	39.2%	40.8%	40.4%
<i>b Interest or Markup Payable (Days)</i>	27.7	60.0	79.2	112.3
<i>c Average Borrowing Rate</i>	14.4%	10.0%	8.0%	5.4%

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

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- (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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