



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
21-Dec-2023	A-	A1	Developing	Maintain	Yes
23-Dec-2022	A-	A1	Stable	Maintain	-
24-Dec-2021	A-	A1	Stable	Maintain	-
24-Dec-2020	A-	A1	Stable	Maintain	-
27-Dec-2019	A-	A1	Stable	Maintain	-
28-Jun-2019	A-	A1	Stable	Maintain	-
28-Dec-2018	A-	A1	Stable	Maintain	-
30-Jun-2018	A-	A1	Stable	Maintain	-

#### Rating Rationale and Key Rating Drivers

EFG Hermes Pakistan Limited ('EFGH' or the 'Company') is a venture of the EFG Hermes Group (the 'Group'), a seasoned financial services group having a presence across multiple countries. As a part of strategic re-allocation of its resources, the Group has declared an exit from Pakistan and has put up its ~51% ownership stake of EFGH for sale. There is an express understanding from the Group to extend financial and non-financial support to the Company in case of any contingency. As a testimony, the Group has already arranged a back-to-back guarantee for long-term loans to the Company amounting to PKR 825mln. Additionally, equity injection of PKR 60mln during 3QCY23 by the Group signifies the Group's ongoing support. The Rating Watch signifies the developing situation of the Group's exit and the potential merger and/or acquisition transaction of EFGH, as notified on the PSX. Market sentiments remained subdued during 1HCY23, with high inflation, economic uncertainty, and rising interest rates lowering investor confidence. However, since the start of 2HCY23, investor confidence has boosted on account of positive macro-economic developments and political stability, raising KSE-100 index to historic highs and elevating market volumes. The ratings incorporate EFGH's strong governance structure and a well-developed matrix organizational structure. A well-qualified and experienced team manages business operations, overseen by Group heads. The Company has a strong internal control framework with Group oversight available in the form of a Group internal audit function. EFGH's operations are concentrated to equity brokerage, whereas MFS and MTS are also present. The Company provides sound research services to its customers while online trading is also available. During 9MCY23, EFGH earned ~PKR 87mln from brokerage revenue (SPLY: ~PKR 93mln). The Company earned an operating profit of ~PKR 9mln on account of ~PKR 104mln gain on sale of proprietary investments. However, the highly leveraged position in a high interest rate environment escalated finance costs to ~PKR 122mln during 9MCY23 (SPLY: ~PKR 78mln), resulting in the Company incurring a loss after tax of ~PKR 101mln during 9MCY23. The Company invests excess cash in low-risk market T-Bills to augment its bottom-line, with the investment book standing at ~PKR 818mln at end-Sep'23. The equity base is considered low, amounting to ~PKR 128mln at end-Sep'23.

Moving forward, the realization of the merger/acquisition transaction shall be critical for the ratings. Meanwhile, continued group support remains vital. Moreover, improvement in topline and profitability is important.

#### Disclosure

<b>Name of Rated Entity</b>	EFG Hermes Pakistan Limited
<b>Type of Relationship</b>	Solicited
<b>Purpose of the Rating</b>	Entity Rating
<b>Applicable Criteria</b>	Methodology   Broker Entity Rating(Aug-23),Methodology   Correlation Between Long-term & Short-term Rating Scales(Jul-23),Methodology   Rating Modifiers(Apr-23)
<b>Related Research</b>	Sector Study   Brokerage & Securities(Jan-23)
<b>Rating Analysts</b>	Hassaan Ahmad   Hassaan.Ahmad@pacra.com   +92-42-35869504

## Profile

**Background** EFG Hermes Pakistan Limited (EFGH), formerly Invest and Finance Securities Limited (IFSL) started its commercial operations in September 1999. The Company is a TREC Holder of the Pakistan Stock Exchange Limited.

**Operations** EFGH primarily provides the services of equity brokerage. The brokerage clients are divided into three broad segments: i) Foreign ii) Institutions and iii) Retail/HNWIs.

## Ownership

**Ownership Structure** EFG Hermes Frontier Holdings LLC is the major shareholder having a 51% holding of EFG Hermes Pakistan. ~5% of shares are held by directors and the rest ~44% are owned by individuals and institutions.

**Stability** EFG Hermes Frontier Holdings LLC is a 100% owned subsidiary of EFG-Hermes Holding S.A.E. The focus of EFG Hermes Frontier Holding LLC is to increase footprints and explore new opportunities in the world's frontier markets. EFG Hermes Holdings S.A.E. is an investment bank in the Middle East, North Africa (MENA) and Pakistan.

**Business Acumen** EFG, also known as the Egyptian Financial Group, became the first investment banking firm in Egypt when it was established by Dr. Mohamed Taymour in 1984. The company brought many investment strategies that were common to the west to Egypt as several of the firm's founders had Wall Street experience in corporate finance, sales & trading and asset management; for example, Hermes established the first equity index in all of Egypt.

**Financial Strength** The sponsors have adequate net worth and may inject capital into the Company with an increasing quantum of operations. The Holding Company earned ~PKR 2,061 mln profit during 9MCY23, while its equity stood at ~PKR 44,107 mln at end Sep'23.

## Governance

**Board Structure** The Company's Board of Directors (BoD) comprises seven members, which include two independent directors and four non-executive directors. Mr. Murad Ansari, a non-executive director, currently chairs the board.

**Members' Profile** The board members on average possess ~20 years of relevant experience. The board members are skilled and experienced in managing business operations efficiently. The presence of independent directors strengthens the governance framework.

**Board Effectiveness** To ensure an effective control environment and compliance with reporting standards, the Company has constituted two board committees: i) Audit Committee, and ii) Human Resource and Remuneration Committee. Both the Audit and Human Resource committees are chaired by independent directors.

**Transparency** Riaz Ahmad Saqib Gohar & Company Chartered Accountants are the external auditors of the company. They have expressed an unqualified opinion on the financial statements for CY22. The firm is QCR rated by ICAP and is in the B Category of SBP's panel of auditors.

## Management

**Organizational Structure** EFGH has a matrix organizational structure that clearly highlights each individual's roles and responsibilities. The functions of the Company are mainly divided into (i) Finance, (ii) Information Technology, (iii) Equity (Sales), (iv) Admin & HR, (v) Research, (vi) Regional Branch, (vii) Risk Management and Customer Services, (viii) Corporate Affairs and Compliance, (ix) Equity (Settlement), (x) Online Sales and (xi) International Sales. The management directly reports to the heads of departments at the group level.

**Management Team** The CEO, Mr. Saad Iqbal, CFA has over 10 years of relevant experience. The CFO, Mr. Ahmad Zakir Hafeez holds MBA and has been associated with the Company since its inception. Mr. Shahid Kamal heading the secretarial and compliance department is an ACMA and also a Fellow Member of PIPFA.

**Management Effectiveness** EFGH's trading system has a centralized real-time risk management system and allows for online trading. The core software functions include Equity Settlement, MM Settlement, Payroll, Accounting and Risk Management. Furthermore, to facilitate its customers, EFGH is establishing a new tailor-made platform which will include an online trading system and a customized mobile app.

**Control Environment** EFGH has established Risk Management procedures for reviewing risk appetite, policies and controls put in place. EFG's internal audit function which is instrumental in mitigating risk is also based at the group level. EFGH has a separate Risk Manager and the policies are aligned at the group level.

## Business Risk

**Industry Dynamics** The brokerage industry faced significant challenges during FY23 due to elevated political uncertainty and soaring inflation, which adversely impacted the country's economic landscape. As a result, market activities were subdued, with investors favoring the security of fixed returns from the higher interest rates prevalent in the economy. However, as FY23 commenced, there emerged a recovery in investor confidence. This can be attributed to the resumption of the IMF program and recent government initiatives aimed at tackling persistent economic issues, including addressing circular debt. Despite these positive trends, the political situation in the country remains unstable, leading many investors to adopt a cautious stance until the conclusion of the elections.

**Relative Position** Despite a decline in market volumes, EFGH has managed to sustain its market share during CY23.

**Revenues** EFGH's operating revenue is mainly concentrated on equity brokerage. Operating revenue comprises only Equity Brokerage Income, Fee and Commission, and Dividend Income. During 9MCY23, the brokerage commission stood at ~PKR 87mln while during 9MCY22 it stood at ~PKR 92 mln. The decrease in the topline is due to increased cost as a result of inflationary pressures, uncontrolled political situation and high interest rate in CY23 when compared with CY22. EFGH's revenue declined by ~8% during 9MCY23 when compared with 9MCY22.

**Cost Structure** The Company's operating and administrative expenses stood at ~PKR 182mln during 9MCY23 (SPLY: ~PKR 144mln). An increase in the amount of debt combined with the increase in market interest rates, resulted in EFGH's finance cost increasing to ~PKR 122mln (SPLY: ~PKR 78mln). As a result of the decline in the top line and surge in finance cost, the Company reported a net loss of ~PKR 101mln during 9MCY23 as compared to a loss of ~PKR 68mln during 9MCY22.

**Sustainability** The Company is focusing on enhancing its Retail Clientele by improving its technology integration as well as its social media presence, while the hiring of additional resources for technological advancement is also under consideration.

## Financial Risk

**Credit Risk** The majority of the credit exposure is with the customers, brokers and other financial institutions. The Company controls its credit risk through a variety of reporting and control procedures, including establishing credit limits based on a review of the counterparties' financial conditions. The Company monitors collateral levels on a regular basis and requests changes in collateral levels as appropriate if considered necessary.

**Market Risk** EFGH, as a matter of policy, does not engage in proprietary equity investments, thus limiting the impact of market risk. The Company invests its excess funds in government securities.

**Liquidity Risk** The current assets of EFGH stood at ~PKR 1,109mln at end-Sept'23 as compared to current liabilities of ~PKR 228mln. The Company retains the ability to borrow funds in the short term and liquidate investments in the financial assets if the need arises.

**Capital Structure** The Company has availed a long-term loan of ~PKR 825mln which is secured against the financial guarantee by the parent company. By the end of 9MCY23, the equity stood at ~PKR 128mln while during CY22, the equity stood at ~PKR 170mln as compared to CY21 (~PKR 163mln).

PKR mln

EFG Hermes Pakistan Limited	Sep-23	Dec-22	Dec-21	Dec-20
	9M	12M	12M	12M

#### A BALANCE SHEET

1 Finances	103	114	80	41
2 Investments	837	840	841	416
3 Other Earning Assets	12	11	11	11
4 Non-Earning Assets	229	223	385	394
5 Non-Performing Finances-net	-	-	-	-
<b>Total Assets</b>	<b>1,181</b>	<b>1,189</b>	<b>1,317</b>	<b>862</b>
6 Funding	825	827	825	715
7 Other Liabilities (Non-Interest Bearing)	229	191	329	11
<b>Total Liabilities</b>	<b>1,054</b>	<b>1,019</b>	<b>1,154</b>	<b>726</b>
<b>Equity</b>	<b>128</b>	<b>170</b>	<b>163</b>	<b>136</b>

#### B INCOME STATEMENT

1 Fee Based Income	105	128	256	172
2 Operating Expenses	(182)	(206)	(196)	(158)
3 Non Fee Based Income	118	103	30	43
<b>Total Operating Income/(Loss)</b>	<b>41</b>	<b>25</b>	<b>90</b>	<b>57</b>
4 Financial Charges	(122)	(112)	(44)	(40)
<b>Pre-Tax Profit</b>	<b>(81)</b>	<b>(86)</b>	<b>47</b>	<b>16</b>
5 Taxes	(20)	(15)	(18)	(15)
<b>Profit After Tax</b>	<b>(101)</b>	<b>(102)</b>	<b>29</b>	<b>2</b>

#### C RATIO ANALYSIS

##### 1 Business Sustainability

Pre Tax Margin	-76.6%	-67.5%	18.2%	9.5%
EBITDA/ Revenue	45.7%	24.1%	37.5%	33.0%
Profit / (Loss) Before Interest & Taxes / Total Assets	3.5%	2.1%	6.9%	6.6%

##### 2 Financial Sustainability

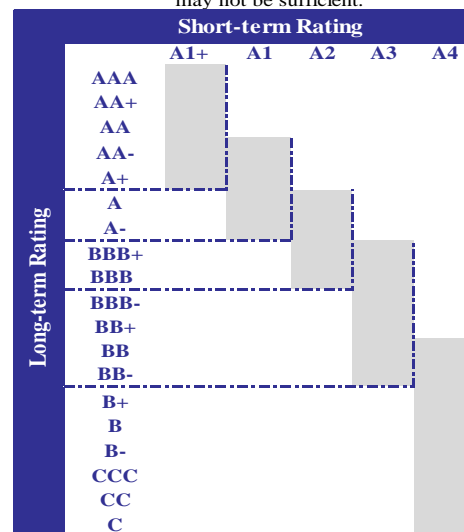
Total Investments / Equity	655.8%	494.1%	515.2%	305.7%
NCB / Equity	0.0%	0.0%	527.9%	276.2%
LCB/ Total Equity	0.0%	487.8%	523.2%	276.2%
( Cash & Cash Equivalents + Government Securities ) / Total Assets	84.0%	83.5%	86.1%	81.8%
Total Debt / Equity	646.3%	486.7%	505.7%	323.9%

### Credit Rating

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.

Scale	Long-term Rating Definition
AAA	<b>Highest credit quality.</b> Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments
AA+	
AA	<b>Very high credit quality.</b> 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-	
A+	
A	<b>High credit quality.</b> 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-	
BBB+	
BBB	<b>Good credit quality.</b> 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.
BBB-	
BB+	
BB	<b>Moderate risk.</b> 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-	
B+	
B	<b>High credit risk.</b> 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-	
CCC	
CC	<b>Very high credit risk.</b> 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.
C	
D	Obligations are currently in default.

Scale	Short-term Rating Definition
A1+	The highest capacity for timely repayment.
A1	A strong capacity for timely repayment.
A2	A satisfactory capacity for timely repayment. This may be susceptible to adverse changes in business, economic, or financial conditions.
A3	An adequate capacity for timely repayment. Such capacity is susceptible to adverse changes in business, economic, or financial conditions.
A4	The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions. Liquidity may not be sufficient.



\*The correlation shown is indicative and, in certain cases, may not hold.

**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 some material identifiable event with indeterminable rating implications. 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 rating 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) the debt instrument is redeemed, c) the rating remains suspended for six months, d) the entity/issuer defaults, or/and e) 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.

**Surveillance.** Surveillance on a publicly disseminated rating opinion is carried out on an ongoing basis till it is formally suspended or withdrawn. A comprehensive surveillance of rating opinion is carried out at least once every six months. However, a rating opinion may be reviewed in the intervening period if it is necessitated by any material happening.

**Note.** This scale is applicable to the following methodology(s):

- a) Broker Entity Rating
- b) Corporate Rating
- c) Debt Instrument Rating
- d) Financial Institution Rating
- e) Holding Company Rating
- f) Independent Power Producer Rating
- g) Microfinance Institution Rating
- h) Non-Banking Finance Companies Rating

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(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)

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- (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 | Clause 11-(A)(p).
- (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)
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- (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)

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- (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 | 17-(a)
- (19) PACRA reviews all the outstanding ratings periodically, on annual basis; Provided that public dissemination of annual review and, in an instance of change in rating will be made; | Chapter III | 17-(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 | 17-(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 | 17-(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 | 14-3(f)(vii)

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