



The Pakistan Credit Rating Agency Limited

Rating Report

EFG Hermes Pakistan Limited | BMR

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Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
28-Dec-2018	BMR2+	-	Stable	Maintain	
02-Mar-2018	BMR2+	-	Stable	Initial	

Rating Rationale and Key Rating Drivers

Broker management rating of EFG Hermes Pakistan Limited represents its association with EFG Group, an international financial services group with presence in eleven countries, and its emerging position in Pakistan's brokerage industry. The rating reflects strong sponsor support and governance at all levels, growing market share, matrix reporting organizational structure and experienced management team of the company.

EFG Hermes Pakistan has a well-developed organizational structure, with clear reporting lines for respective heads at the group level. It is the first brokerage house in the country with a designated foreign sales team operating from UAE office. The research department draws strength from the experience of EFG Group as the company emphasize on providing high quality market reports to its clients in a systematic way. The IT infrastructure allows full integration of the front and back office functions, allowing generation of real time reports. The company offers online trading features and has recently launched its mobile app. As a group policy, the company does not invest in equity market and all investments have been deployed in government backed debt securities.

The rating is dependent upon the company's management to fully align the company with the group policies in timely fashion. Optimizing market share and retention of key human resource remains critical for the rating.

Disclosure

Name of Rated Entity	EFG Hermes Pakistan Limited BMR
Type of Relationship	Solicited
Purpose of the Rating	Broker Management Rating
Applicable Criteria	Methodology Broker Management Rating(Jun-18)
Related Research	Sector Study Brokerage & Security(Nov-18)
Rating Analysts	Shahzaib Khalid shahzaib.khalid@pacra.com +92-42-35869504



Ownership

Ownership Structure EFG Hermes Pakistan Limited is a subsidiary of EFG Hermes Frontier Holdings LLC, which controls 51% stake in EFG Pakistan. The ultimate owner of the group is EFG Hermes Holding S.A.E (Egyptian Financial Group Hermes Holding Company). A group of professionals including the ex-CEO, owns around 27%, while the remaining stake is held by the general public.

Stability The ownership structure is stable as the company is a subsidiary of EFG Hermes Frontier Holdings LLC, an EFG group company.

Business Acumen EFG Hermes Holding S.A.E., established in 1984, is an Egyptian investment bank specializing in securities brokerage, asset management, investment banking and private equity. EFG Hermes is listed on the Egyptian Exchange (EGX) and London (LSE) Stock Exchange. EFG Hermes has offices in eleven countries including Pakistan and serve clients from the Middle East, North Africa, Europe and the United States.

Financial Strength EFG Hermes Holding S.A.E.'s equity stood at ~EGP 13.9bln (~USD 0.8bln) as at the end of CY17. The group made net profit of ~EGP 1.25bln (~USD 0.1bln) in CY17.

Governance

Board Structure EFG Pakistan has a 14 member board of directors. The Chairman and CEO included, six directors are key management personnel of EFG Group.

Members' Profile Mr. Murad Ansari is the Chairman of EFG Pakistan and he is also the co-head of the MENA financials team of EFG Hermes Frontier Holdings LLC. He holds a MBA from Institute of Business Administration and carried sixteen years of professional experience in equity research and sales. All other board members are highly qualified and professionally accomplished individuals.

Board Effectiveness EFG Pakistan has two board committees, namely i) Audit Committee and ii) HR and remuneration committee. TOR's for both committees are well defined. Audit committee meets on quarterly basis to review the financial statements and internal audit findings. Audit committee is chaired by an independent director.

Financial Transparency Internal audit function of EFG Pakistan is performed by the parent company. The company's external auditors are AGN Riaz Ahmad Saqib Gohar & Co, ranked under category "B" as per the SBP rankings. The auditor's issued an unqualified opinion on the financial statements of EFG Pakistan for the year ended CY17 and period ended 9MCY18.

Management

Management Team The company's CEO resigned in the second half of CY18 and was replaced by Mr. Shahid Kamal as the acting CEO. Mr. Shahid Kamal (ACMA, FPFA) has diverse experience of more than a decade in risk management, internal audit and compliance. Mr. Ahmad Zakir Hafeez is the current CFO of the company. He has been associated with the company since 1999. Retention and removal of key management personnel is critical.

Organizational Structure For effective management integration, matrix reporting structure is in place. Key departmental heads have reporting line to respective functions at group level, in addition to reporting to the CEO. This structure provides better oversight while bringing broader exposure and experience to local operations.

Client Servicing EFG Pakistan offers multiple account opening mediums. A number of value added services are offered to clients including online trading, research portal and mobile app. To attract customers, investor awareness programs, including road shows in foreign countries, are conducted by the company. The company has a strong client reporting mechanism with account statements and market reports communicated to the clients on regular basis.

Complaint Management The company has sound complaint management system in place. Complaints can be made via email and phone call. The compliance department oversees the complaint handling process.

Extent Of Automation / Integration EFG Pakistan utilizes one of the best trading softwares "Trade Cast" available to the brokerage industry in the country. The front office software has real time synchronization with the back office ensuring timely reporting for users at all levels.

Continuity Of Operations To ensure business continuity in unforeseen circumstances, EFG Pakistan has formulated an intricate disaster recovery and continuity plan.

Risk Management Framework The group is implementing its policies and procedures at EFG Pakistan through multiple trainings. To avoid market risk, the company has devised a policy for not taking proprietary stock market exposure. Major developments in the KYC procedures minimizes the credit risk of the company.

Regulatory Compliance The company's regulatory compliance revolves around the group risk management and compliance policies in addition to the local legislative requirements. The risk management & compliance department ensures that all the regulatory requirements are fulfilled on timely basis.

Business Sustainability

Business Risk CY18 started off with a slightly bull run with KSE-100 posting a positive cumulative return ~4% in the first half of the year. After the general elections in July 18, the political uncertainty minimized. However, the investors remained cautious due to falling central bank reserves and balance of payment crises that resulted in KSE-100 posting a negative return of ~3% in the 3rd quarter of CY18. The overall trading volumes in FY18 remained quite low (FY18: 84mln, FY17: 140mln) as compared to previous year. This put pressure on income of all brokerage entities.

Business Profile Primary activities of the company includes equity brokerage and research. In terms of value of traded shares, the company enjoys ~5% market share.

Revenue And Profitability Analysis The company's operating revenue mainly comprises equity brokerage income and inter-bank brokerage. During 9MCY18, equity brokerage decreased by ~10% to ~PKR 89mln and operating expenses increased by ~2% to ~PKR 117mln as compared to SPLY. Following the industry wide loss trend, the company suffered net loss of ~PKR 29mln in 9MCY18. Going forward, the management intends to leverage its brand to capture maximum market share as activity in stock market picks up

Financial Sustainability

Credit Risk EFG Pakistan has due diligence procedures in addition to KYC, for the assessment of its client creditworthiness. Applicable policies for leveraged products have been adopted and limits have been defined, which are strictly monitored.

Market Risk EFG Pakistan carries no market risk as the group policy prohibits it from having a proprietary book of listed equities. The investment book is completely deployed in government debt securities.

Liquidity Profile The company has a long term loan from a bank in the UAE. The funds have been primarily utilized to finance the investment book and the rest has been used in financing the leveraged products. The loan facility has been secured against an irrevocable and unconditional financial guarantees provided by the parent company to the bank. In addition, the company also has bank lines from local banks of ~PKR 650 million. Furthermore, liquid assets of the company were 5x of the trade liabilities as at end 9MCY18 (Dec 17: 2.1x).

Financial Risk EFG Pakistan has a leveraged capital structure, However, guarantee provided by the parent company against the loan obtained from the foreign bank provides comfort. The company's Net Capital Balance stood at ~PKR 441mln as at end 9MCY18 (Dec-17: ~705mln). The company can carry an exposure of up to 25x of its NCB.



The Pakistan Credit Rating Agency Limited

EFG Hermes Pakistan Limited

PKR Mn

BALANCE SHEET

	30-Sep-18 <i>Unaudited (9MCY18)</i>	31-Dec-17 <i>Audited (2HCY17)</i>	30-Jun-17 <i>Audited (FY17)</i>	30-Jun-16 <i>Audited (FY16)</i>
EARNING ASSETS				
1 Finances	99	178	76	-
2 Investments	317	259	616	88
	416	437	692	88
NON-EARNING ASSETS				
3 Cash and Bank Balances - Client funds	59	99	99	48
4 Trade debts	21	51	86	33
5 Advances, Deposits and Other receivables	154	191	197	72
6 Others (including Fixed Assets)	36	41	35	35
TOTAL ASSETS	686	820	1,109	276
7 Equity	201	240	256	192
8 Borrowings	378	472	718	6
Other Liabilities (Non-Interest Bearing)				
9 Trade Creditors*	72	73	90	46
10 Other Liabilities	35	36	46	32
TOTAL EQUITY & LIABILITIES	686	820	1,109	276

Proportionated for 9MCY18 and CY17

INCOME STATEMENT

	30-Sep-18 <i>Unaudited (9MCY18)</i>	31-Dec-17 <i>Audited (2HCY17)</i>	30-Jun-17 <i>Audited (FY17)</i>	30-Jun-16 <i>Audited (FY16)</i>
Fee Based Revenue				
11 Advisory	-	-	-	-
12 Brokerage	97	76	124	75
Operating Expenses				
13 Personnel Expenses*	(63)	(42)	(75)	(51)
14 Administrative Expenses*	(54)	(39)	(55)	(38)
Fee Based Income / (Loss)	(20)	(4)	(6)	(13)
Non Fee-Based Income				
15 Bank Deposits and others	-	-	-	-
16 Gain on Sale of Investments	10	4	56	3
17 Others	14	13	4	6
Total Operating Income / (Loss)	4	13	55	(5)
18 Financial Charges	(20)	(16)	(9)	(1)
Profit / (Loss) Before Tax	(16)	(3)	45	(6)
19 Taxes	(12)	(8)	(8)	(4)
Net Income	(29)	(11)	37	(10)

RATIO ANALYSIS

	30-Sep-18 <i>Unaudited (9MCY18)</i>	31-Dec-17 <i>Audited (2HCY17)</i>	30-Jun-17 <i>Audited (FY17)</i>	30-Jun-16 <i>Audited (FY16)</i>
CREDIT RISK				
20 Accounts Receivable / (Short Term Borrowings + Customer Advances + Accounts Payable)	28.9%	31.1%	56.4%	68.6%
LIQUIDITY RISK				
21 Trade Receivables / Trade Payables	0.3	0.7	1.0	0.7
22 Liquid Assets / Trade Related Liabilities	5.2	4.9	8.0	2.9
23 Liquid Assets / (Short term Borrowings + Advances from Customers + Accounts Payable)	5.2	2.2	4.7	2.9
COVERAGES				
24 EBITDA/Gross Interest	-7.7	-12.5	33.4	-54.7
25 FCFO/Gross Interest	-15.6	-66.8	19.5	-235.4
BUSINESS RISK				
26 Net Profit (before tax) Margin	n/m	n/m	36.7%	n/m
27 Trade Debtors	80.2%	81.2%	67.2%	89.9%
28 Operating Cost-to-Total Income	97.0%	85.9%	70.2%	106.1%
29 Net Fee based Income to Net Profit before Tax	123.8%	152.1%	n/m	227.7%
30 Net Profit (before tax) to Total Income	n/m	n/m	24.6%	n/m
31 Net Non-Earning Assets / Equity	116.7%	144.6%	145.1%	81.1%
FINANCIAL RISK				
32 Borrowings / Equity	187.8%	196.6%	280.5%	3.0%
33 NCB / Equity	-	188.2%	275.3%	28.2%

** Proportionated in 9MCY18*

BROKER MANAGEMENT RATING SCALE

SYMBOL	DEFINITION	
BMR 1A	Excellent	Excellent regulatory compliance, control environment, and financial management; governance and risk management frameworks are extremely effective; HR, IT, and customer services are strongly proactive.
BMR 1++ BMR 1+ BMR 1	Strong	Strong regulatory compliance, control environment, and financial management; governance and risk management frameworks are highly effective; HR, IT, and customer services are highly proactive.
BMR 2++ BMR 2+ BMR 2	Sound	Sound regulatory compliance, control environment, and financial management; governance and risk management frameworks are effective; HR, IT, and customer services are proactive.
BMR 3++ BMR 3+ BMR 3	Adequate	Adequate regulatory compliance, control environment, and financial management; governance and risk management frameworks are satisfactory; HR, IT, and customer services are adequate.
BMR 4++ BMR 4+ BMR 4	Inadequate	Inadequate regulatory compliance, control environment, and financial management; governance and risk management frameworks need improvements; HR, IT, and customer services are insufficient.
BMR 5	Weak	Weak regulatory compliance and business practices.

SURVEILLANCE AND VALIDITY OF THE RATING

PACRA shall not keep the Broker Management Rating under constant surveillance. The rating will be reviewed at least once every six months. Any material happening during a period that may warrant a revision of rating will be incorporated in the following review.

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'.

WITHDRAWN

A rating is withdrawn on a) termination of rating mandate, or b) cessation of underlying entity.

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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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- (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)

Independence & Conflict of interest

- (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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