The Pakistan Credit Rating Agency Limited

Rating Report

MAAKSONS ENGINEERING CORPORATION LIMITED

Report Contents

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Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
24-Aug-2021	BBB+	A2	Stable	Maintain	-
25-Aug-2020	BBB+	A2	Stable	Maintain	-
27-Aug-2019	BBB+	A2	Stable	Maintain	-
28-Feb-2019	BBB+	A2	Stable	Initial	-

Rating Rationale and Key Rating Drivers

Maaksons Engineering Corporation Limited (Maaksons) has been in the construction industry for many decades. The company has three generations of the sponsoring family in the business and has two main offices – Lahore and Islamabad. The sponsors have a very good understanding of the business. The reporting and functional responsibilities are clearly demarcated. Maaksons has a no limit contract license. The Company has a track record with strong capabilities in executing turnkey projects. Maaksons is re – strategizing its business model and has built a portfolio of properties which are diverse and furnish different propositions to translate them into revenue streams. Going forward Maakson's approach is to reduce reliance on contractual business by developing owned properties for commercial and residential purposes at company and group level, with a view to ensure revenue sustainability in the future. Maaksons will follow a hybrid business model whereby partial area will be sold on plan basis, while the remaining will be retained and operated on rental basis. Maaksons has redefined strategy of building assets, required for its operations as well as investment purpose, through surplus cash. Occasionally, funded facilities are also utilized to finance acquisition. Currently, the company is adequately leveraged, has a mix of funded and non-funded banking lines to facilitate its business.

The ratings incorporates inherent synergies and diversification in the group structure providing implicit strength to the business model. Going forward successfully completion of contracts on time and envisaged strategy of sustainable revenue stream for development of properties remains pivotal for considerable growth. Good corporate governance practice is considered essential.

Disclosure

Name of Rated Entity	MAAKSONS ENGINEERING CORPORATION LIMITED
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology | Corporate Rating(Jun-21),Criteria | Correlation Between Long-term & Short-term Rating Scales(Jun-21),Criteria | Rating Modifiers(Jun-21)
Related Research	Sector Study | Construction(Mar-21)
Rating Analysts	Saadat Mirza | saadat.mirza@pacra.com | +92-42-35869504

Profile

Legal Structure Maaksons Engineering Corporation Limited (MAAKSONS), previously known as M. A. Aleem Khan & Sons (Pvt) Limited, was officially registered as a Private Limited Company in 1984 but has been in business since 1951.

Background The Company commenced its business in 1951 with Public Works Development Authority and Irrigation Department thus successfully completing various projects of water management and irrigation systems. MAAKSONS scope of work comprises of construction of Roads and Highways, Bridges & Structures, Residential and Commercial Buildings, Canals and Tunnels, etc.

Operations Presently the Company holds “no limit” C-A license from Pakistan Engineering Council. Different license codes range from C-6 to C-A based on the contract value allowed to undertake within that contract band. Significant projects to its credit are Signal Free Corridor on Islamabad Highway and in DHA Lahore, Metro Lahore, 29 storey Telecom Tower Islamabad, Gulberg Green, 3x210 Thermal Power Station Muzaffargarh, Chashma Canal, etc. to name a few.

Ownership

Ownership Structure Mr. M. Aleem Khan, the founder of the company is identified as the man at the last mile and is entrusted with the oversight of the entire business.

Stability MAAKSONS is entirely a family owned business where the third generation has also joined in the recent years. The hierarchy has clear lines of authority terminating at the MD. His two sons and grandsons look after their respective areas. The two sons of M Nadeem Khan, Shehzer Khan and Shahnawaz Khan took over the ownership from their mother and aunt in 2016.

Business Acumen The sponsoring family has been in the construction industry for over four decades with the MD having 60+ years of rich industry experience. The sponsors have a thorough understanding of the business as they are all actively involved in the running of the day to day affairs.

Financial Strength MAAKSONS has an adequate financial profile. The entity has a few subsidiaries, namely, MAAKCRETE, MAAK Asphalt, and MAAK Gas which have the main purpose of serving the parent organization. They are trying to diversify their business somewhat by entering into the real estate projects, agriculture and dairy industry and also own MAAK Agro and MAAK Farms.

Governance

Board Structure The overall control of the company vests in three senior directors; MD and his two sons. Out of the 9 shareholders, seven male members of the family are executive directors whereas the two daughters-in-law of Mr M Aleem Khan are silent partners. There is no independent director on the board, hence the governance structure needs improvement.

Members’ Profile All of the board members carry extensive experience of the construction industry. The two sons of M. Aleem Khan, M Waseem Khan and M Nadeem Khan joined the business in 1980s and have more than four decades of experience.

Board Effectiveness The Board members are actively involved in the planning and execution of the business projects and overseeing the operations on a regular basis.

Financial Transparency An independent director on the Board would ensure effective, transparent and independent oversight of the company’s operations. The governance model is weak and needs improvement in order to comply with the corporate governance model. The company is in the practice of forming quarterly accounts. M/s. Kamran & Co. Chartered Accountants is the external auditor of the company and has expressed qualified audit opinion on the financial statements for the year ended June 30th, 2020 for not booking the super tax liability, as the case is at appellate stage.

Management

Organizational Structure The company operations are divided into two regions, Islamabad and Lahore, which operate independently under the oversight of MD/Chairman M A Aleem Khan. Company head office is in Lahore while in Islamabad is the regional office. Business pertaining to Lahore region is under the management of M Waseem Khan and his two sons.

Management Team MAAKSONS has a team of experienced and competent professionals who have been with the entity over a long period of time.

Effectiveness Functions of the management are clear and well-defined to effectively achieve its underlying goals and objectives. System of internal control is in place, although continuous review of these controls by an internal audit department would ensure further effectiveness of the management.

MIS MAAKSONS is currently using Axiom ERP System for generating daily reports in order to track project specific progress. It is a web based system which is accessible to all the staff working on project and generates reports on supplier, procurement, and inventory etc.

Control Environment MAAKSONS adheres to strict quality control standards as it is the need of the construction industry. The company maintains a comprehensive MIS reporting system for the management to keep track of its different project sites and activities.

Business Risk

Industry Dynamics The construction sector share in GDP for FY19-20 recorded an uptick of 2.85% from the previous year (FY18-19: 2.82%). This status quo contribution is on account of the economic slowdown which was experienced due to the globally declared pandemic - Covid19. There are a number of other factors that have been slowing growth, including GoP insignificantly increase the PSDP funding, growing inflation, and interest rates. However now the Govt. has taken major infrastructure projects under the Naya Lahore scheme and Naya Pakistan Housing Scheme which will kick the economic activity along with CPEC near completion and there will be a lot more clarity on the economy's direction in the upcoming fiscal years.

Relative Position Out of the 10,000+ firms registered with Pakistan Engineering Council as Constructors / Operators, only ~100 (1%), including MAAKSONS, hold the prestigious CA category (no limit) license which enables them to be on the pre-qualifying list of approved constructors.

Revenues MAAKSONS has multiple DHA Lahore based projects with expected good amount of return. For 1HFY21, revenue stood at PKR 801mln (FY20: PKR 2bln; FY19 PKR 3.3bln) although there are projects in pipeline which would add to the topline in the upcoming year.

Margins Like other companies in the construction industry, MAAKSONS has also experienced an erratic and less predictable topline primarily due to project based contractual nature of revenue. Finance cost reduced to PKR 41mln at the end of 1HFY21 as government has slashed the policy rate during FY21. Henceforth, MAAKSONS posted a net profit of PKR 239mln (1HFY20: PKR 75mln; FY20: PKR 106mln; FY19: PKR 184.6mln) due to better control over expenses.

Sustainability Given the slowdown in the economic activity and drastic impacts of COVID-19, maintaining a continued healthy business pipeline remains a challenge. After the pandemic, the revival of the industry is based upon the Govt. planned massive infrastructural projects wherein; the company is working with Governmental bodies which assures the credibility of projects and future prospect.

Financial Risk

Working Capital For working capital needs, which is a function of inventory and receivables, a company relies on both internal cash flows as well as short term borrowing (STB). MAAKSONS working capital management is good with improving negative net working capital days 1HFY21: -28days (FY20: -67days; FY19: -84 days) which has continued. During 1HFY21, MAAKSONS reduced the utilization of short term borrowings which stood at PKR 882mln from PKR 1,229mln resulting in reducing in short-term total leverage of the company (improve the room to borrow).

Coverages During 1HFY21, MAAKSONS free cash flows (FCFO), amounted to PKR 177mln (FY20: PKR 350mln; FY19: PKR ~383mln). Interest coverage ratio has been improved to 5.2 during the period, however, it would deteriorate if additional business isn’t realized in the coming periods.

Capitalization At end FY20, the company had a slightly leveraged capital structure, with a debt to debt plus equity ratio of 26% (FY19: 27%). Major portion of debt comprises STB. During 1HFY21, the debt to debt plus equity ratio moved to 19% and debt stood at PKR 943mln (FY20: 1,289mln; FY19; 1,092mln).

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Financial Summary
PKR mln

Maaksons Engineering Corporation Ltd	Dec-20	Jun-20	Jun-19	Jun-18
Construction	6M	12M	12M	12M
A BALANCE SHEET				
1 Non-Current Assets	2,594	2,866	2,337	1,841
2 Investments	436	506	482	486
3 Related Party Exposure	497	497	557	550
4 Current Assets	1,967	2,008	2,206	2,771
a Inventories	-	-	-	-
b Trade Receivables	*296*	*308*	*249*	*369*
5 Total Assets	5,494	5,876	5,581	5,648
6 Current Liabilities	575	851	1,552	2,359
a Trade Payables	*345*	*504*	*793*	*1,354*
7 Borrowings	943	1,289	1,092	537
8 Related Party Exposure	-	-	-	-
9 Non-Current Liabilities	-	-	-	-
10 Net Assets	3,976	3,736	2,937	2,752
11 Shareholders' Equity	3,976	3,736	2,937	2,752
B INCOME STATEMENT				
1 Sales	801	2,001	3,308	5,299
a Cost of Good Sold	*(633)*	*(1,531)*	*(2,788)*	*(4,399)*
2 Gross Profit	168	470	520	900
a Operating Expenses	(28)	(113)	(167)	(139)
3 Operating Profit	139	357	353	761
a Non Operating Income or (Expense)	*197*	*3*	*185*	*4*
4 Profit or (Loss) before Interest and Tax	336	360	537	765
a Total Finance Cost	*(41)*	*(162)*	*(123)*	*(55)*
b Taxation	*(56)*	*(91)*	*(229)*	*(372)*
6 Net Income Or (Loss)	239	106	185	337
C CASH FLOW STATEMENT				
a Free Cash Flows from Operations (FCFO)	*177*	*350*	*383*	*517*
b Net Cash from Operating Activities before Working Capital Changes	*122*	*188*	*286*	*460*
c Changes in Working Capital	*(161)*	*(619)*	*(627)*	*132*
1 Net Cash provided by Operating Activities	(39)	(431)	(341)	592
2 Net Cash (Used in) or Available From Investing Activities	466	148	(198)	(337)
3 Net Cash (Used in) or Available From Financing Activities	(346)	116	458	(230)
4 Net Cash generated or (Used) during the period	81	(168)	(81)	25
D RATIO ANALYSIS				
1 Performance				
a Sales Growth (for the period)	-20.0%	-39.5%	-37.6%	64.6%
b Gross Profit Margin	20.9%	23.5%	15.7%	17.0%
c Net Profit Margin	29.9%	5.3%	5.6%	6.4%
d Cash Conversion Efficiency (FCFO adjusted for Working Capital/Sales)	2.0%	-13.5%	-7.4%	12.2%
*e Return on Equity [Net Profit Margin * Asset Turnover * (Total Assets/Sh*	11.6%	2.9%	6.2%	13.4%
2 Working Capital Management				
a Gross Working Capital (Average Days)	69	51	34	18
b Net Working Capital (Average Days)	-28	-67	-84	-49
c Current Ratio (Current Assets / Current Liabilities)	3.4	2.4	1.4	1.2
3 Coverages				
a EBITDA / Finance Cost	5.2	3.0	5.5	17.3
b FCFO / Finance Cost+CMLTB+Excess STB	4.4	1.4	0.8	3.3
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)	0.2	0.7	1.6	0.3
4 Capital Structure				
a Total Borrowings / (Total Borrowings+Shareholders' Equity)	19.2%	25.6%	27.1%	16.3%
b Interest or Markup Payable (Days)	71.2	71.0	107.3	55.3
c Entity Average Borrowing Rate	6.5%	12.1%	13.9%	1.0%

Credit Rating

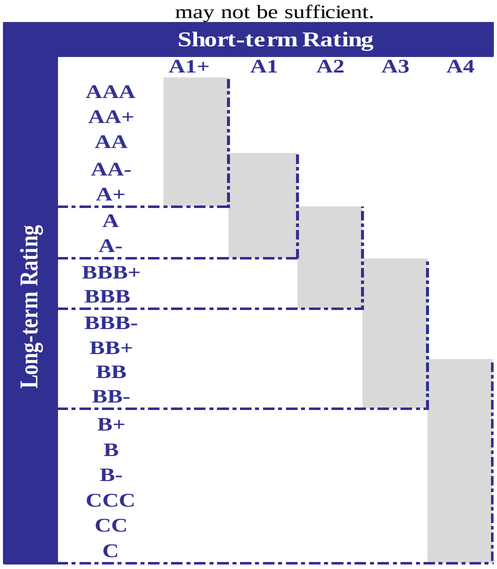
Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

Long-term Rating

Scale	Definition
AAA	**Highest credit quality.** Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments
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.
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.
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.
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+ 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.
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.

Short-term Rating

Scale	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
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 surveill 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):

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

Instruments
a) Basel III Compliant Debt Instrument Rating
b) Debt Instrument Rating
c) Sukuk Rating

Regulatory and Supplementary Disclosure
(Credit Rating Companies Regulations,2016)

Rating Team Statements
(1) Rating is just an opinion about the creditworthiness of the entity and does not constitute recommendation to buy, hold or sell any security of the entity rated or to buy, hold or sell the security rated, as the case may be | Chapter III; 14-3-(x)

2) **Conflict of Interest**
i. The Rating Team or any of their family members have no interest in this rating | Chapter III; 12-2-(j)
ii. PACRA, the analysts involved in the rating process and members of its rating committee, and their family members, do not have any conflict of interest relating to the rating done by them | Chapter III; 12-2-(e) & (k)
iii. The analyst is not a substantial shareholder of the customer being rated by PACRA [Annexure F; d-(ii)] Explanation: for the purpose of above clause, the term "family members" shall include only those family members who are dependent on the analyst and members of the rating committee

Restrictions
(3) No director, officer or employee of PACRA communicates the information, acquired by him for use for rating purposes, to any other person except where required under law to do so. | Chapter III; 10-(5)
(4) PACRA does not disclose or discuss with outside parties or make improper use of the non-public information which has come to its knowledge during business relationship with the customer | Chapter III; 10-7-(d)
(5) PACRA does not make proposals or recommendations regarding the activities of rated entities that could impact a credit rating of entity subject to rating | Chapter III; 10-7-(k)

Conduct of Business
(6) PACRA fulfills its obligations in a fair, efficient, transparent and ethical manner and renders high standards of services in performing its functions and obligations; | Chapter III; 11-A-(a)
(7) PACRA uses due care in preparation of this Rating Report. Our information has been obtained from sources we consider to be reliable but its accuracy or completeness is not guaranteed. PACRA does not, in every instance, independently verifies or validates information received in the rating process or in preparing this Rating Report.
(8) PACRA prohibits its employees and analysts from soliciting money, gifts or favors from anyone with whom PACRA conducts business | Chapter III; 11-A-(q)
(9) PACRA ensures before commencement of the rating process that an analyst or employee has not had a recent employment or other significant business or personal relationship with the rated entity that may cause or may be perceived as causing a conflict of interest; | Chapter III; 11-A-(r)
(10) PACRA maintains principal of integrity in seeking rating business | Chapter III; 11-A-(u)
(11) PACRA promptly investigates, in the event of a misconduct or a breach of the policies, procedures and controls, and takes appropriate steps to rectify any weaknesses to prevent any recurrence along with suitable punitive action against the responsible employee(s) | Chapter III; 11-B-(m)

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)

Proprietary Information