The Pakistan Credit Rating Agency Limited

ETIMAAD ENGINEERING (PRIVATE) LIMITED

	NEW [JUNE-17]	INITIAL [JUNE-16]
Long-Term	BB+	BB+
Short-Term	A3	A3
Outlook	Stable	Stable

REPORT CONTENTS

JUNE 2017

Profile &Ownership

- Etimaad Engineering Private Limited (Etimaad), established in May 2007, is an integrated engineering and consultancy services provider, operating with its head office in Lahore.
- There are two subsidiaries of Etimaad named "Etimaad Manufacturing (Private) Limited" and "One Tree Hill (Private) Limited", however both entities are not operational.
- Etimaad had an investment through a joint venture in Middle East named Arabian Etimaad Industrial Company. This has been sold in FY15.
- Mr. Mazharuddin Ansari and Mr. Laeequddin Ansari, experienced professionals in local engineering industry, own 81% stake in Etimaad directly and indirectly through other family members. Remaining stake lies with fellow alliances of key sponsors who left the company in past years.

Governance

- BoD comprises three members including the CEO.
- Mr. Mazharuddin-Ansari, the Chairman, is the key founder of Etimaad. He carries more than four decades of engineering experience in renowned local and foreign organizations.
- Mr. Suhail Shafique – Vice Chairman is a chemical engineer by profession. He has 25 years of experience in renowned engineering services organizations.
- All board members carry executive roles in the company; thus lacking independent oversight at board level

Management and Systems and Control

- Mr. Farooq Hussain Mughal is appointed as CEO in FY15. He has worked with Etimaad as CFO and then COO previously. As he is new to his current role with responsibility of overall operations, support from senior executive members, Chairman and Vice-chairman, provides comfort.
- Management team is experienced.
- The company has an integrated financial, cost control and project management system, further strengthening of these is important with expected growth in business operations.

Business Risk

- Revenues of construction business dependent on developmental activities, while bottom-line performance is subject to quality selection and execution ability.
- The topline of Etimaad remained volatile. However, during FY16, volatility stayed in positive bound to result in an increase of ~40% on YoY basis.
- Higher proportion of construction contracts in the revenue mix (FY16: 66%; FY15: 58%; FY14: 30%) consequently recurring business has lower contribution in topline
- The company operates on thin margins. During FY16, gross margins improved on YoY basis (FY16: 18.4%; FY15: 5.2%, FY14: 0.8%).
- Finance cost increased to 3%, while in absence of any considerable capital gain (FY15: PKR 113mln) bottom line rested at PKR 20mln (FY15: PKR 24mln; FY14: loss of PKR 59mln).
- Losses in major projects in the past, namely Shahbaz Air Base, NPT-Aiwan-e-Quaid-e-Azam and Aisha Steel Mills; the management's expectation of some recovery is yet to be materialized.
- Going forward, while targeting growth, the management visions Etimaad's stability over the long-term. The management's ability to improve its bottom-line performance by identifying and executing profitable projects is critical.

Financial Risk

- Long working capital cycle (FY16: 194 days; FY15: 240 days; FY14: 417 days) is a drag on management of short-term finance.
- Operating cash flows (FCFO) - a function of profitability stabilized (FY16: 70mln; PKR FY15: PKR -53mln; FY14: PKR - 22mln). Hence, Coverages, previously negative, became positive at 2.7%.
- Although Etimaad's capital structure is adequately leveraged (debt to debt plus equity ratio: end-Jun 16: 43%; end-Jun15: ~42%; end-Jun14: ~46%), due to suppressed cash flows the company's short-term finances are secured by sponsor's support – personal guarantees and certain assets of sponsors.

RATING RATIONALE

Etimaad, engaged in providing engineering, procurement, construction and maintenance services, was established in 2007. The Company's profile draws strength from its experienced management team. Over the years, the sponsors established similar businesses mainly in Saudi Arabia (subsidiary) and Qatar (associate). Considering worsening market conditions due to geopolitical tensions in the region and the turmoil in oil prices, Etimaad decided to divest its shares and continued its focus in Pakistan. Etimaad has completed various projects in Pakistan and overseas. Etimaad has a reasonable universe of contracts on its plate, wherein margins are adequate. The performance of the company resonates with contracts in hand. The business strategy envisages enhanced focus on EPC in power sector; bagasse based power plants. The financial stream is stressed given limited cash flow stream and Etimaad's need to avail bank guarantees for awarded projects. Herein, financial support of sponsors in essential.

The sponsors demonstrated their commitment by operationally supporting the business and providing, i) fresh capital whenever the need arose, and ii) security and personal guarantees to obtain financial facilities and guarantees.

In the recent past, the management has undertaken several initiatives to streamline its business. These include, i) sale of foreign operations to increase focus on local business, ii) organizational restructuring, and iii) revamping of overall business model in line with market dynamics with a strategic focus on subcontracting. The management is confident that the financial profile will gradually gain strength through organic growth. At the same time, the management remains focused to settle disputes and recover receivables to minimize deficit in projects where the company had incurred losses.

KEY RATING DRIVERS

The success of the management's initiatives is critical for prosperity of the company. Meanwhile, strengthening of governance structure is important which can be achieved by induction of non-executive member(s) on the Board.

Etimaad Engineering (Private) Limited

PKR (mln)

BALANCE SHEET	31-Mar-17	30-Jun-16	30-Jun-15	30-Jun-14
	9MFY17	FY16	FY15	FY14
Non-Current Assets	**171**	**178**	**177**	**199**
Investments (Incl. associates)	**3**	**3**	**3**	**24**
Equity	3	3	3	24
Debt	-	-	-	-
Current Assets	**996**	**1,029**	**962**	**941**
Inventory	436	402	398	476
Trade Receivables	353	377	308	287
Others	207	251	256	178
Total Assets	**1,170**	**1,210**	**1,142**	**1,165**
Debt	**271**	**255**	**232**	**256**
Short-term	189	155	204	199
Long-term (Inlc. Current Maturity of long-term debt)	82	100	27	58
Other shortterm liabilities	448	511	485	499
Other Longterm Liabilities	6	6	4	3
Shareholder's Equity	**444**	**438**	**421**	**406**
Total Liabilities & Equity	**1,170**	**1,210**	**1,142**	**1,165**

PKR (mln)

INCOME STATEMENT				
Turnover	**551**	**897**	**643**	**413**
Gross Profit	117	165	33	3
Other Income	0	(2)	113	40
Financial Charges	(18)	(26)	(27)	(44)
Net Income	**7**	**20**	**24**	**(59)**

Cashflow Statement				
Free Cashflow from Operations (FCFO)	38	70	(53)	(22)
Net Cash changes in Working Capital	(58)	(90)	38	(16)
Net Cash from Operating Activities	(38)	(47)	(44)	(80)
Net Cash from InvestingActivities	(9)	(22)	128	105
Net Cash from Financing Activities	16	23	(32)	(8)

Ratio Analysis				
Performance				
Turnover Growth	-18.8%	39.5%	55.6%	-9.0%
Gross Margin	21.2%	18.4%	5.2%	0.8%
Net Margin	1.3%	2.3%	3.8%	-14.2%
ROE	2.1%	4.7%	5.8%	-14.4%
Coverages				
Interest Coverage (FCFO/Gross Interest)	2.1	2.7	-2.0	-0.5
Core: (FCFO/Gross Interest+CMLTD+Uncovered Total STB)	1.0	1.3	-1.0	-0.3
Total: (TCF) / (Gross Interest+CMLTD+Uncovered Total STB)	1.0	1.3	-1.0	-0.3
Debt Payback (Total LT Debt Including UnCovered Total STBs) / (FCFO- Gross Interest)	4.4	2.4	-0.4	-1.0
Liquidity				
Net Cash Cycle (Inventory Days + Receivable Days - Payable Days)	260.2	193.7	240.2	417.0
Capital Structure (Total Debt/Total Debt+Equity)	43.5%	42.5%	41.5%	45.8%

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

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 RATINGS

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.

B: The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions.

C: An inadequate capacity to ensure timely repayment.

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 surveill the opinion due to lack of requisite information

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Regulatory and Supplementary Disclosure

Name of Issuer — Etimaad Engineering (Private) Limited
Sector — Enginnering
Type of Relationship — Solicited

Purpose of the Rating — Independent Risk Assessment

Rating History

Dissemination Date	Long Term	Short Term	Outlook	Action
13-Jun-17	BB+	A3	Stable	Maintain
13-Jun-16	BB+	A3	Stable	Initial

Related Criteria and Research
Related Research — Engineering, Procurement and Construction - View Point | Jun -17
Rating Methodology — Corporate Rating Methodology

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Rating Team Statement

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