The Pakistan Credit Rating Agency Limited

HABIB CONSTRUCTION SERVICES (PUBLIC) LIMITED
RATING REPORT

	INITIAL [DEC-17]
Entity	
Long Term	A-
Short Term	A2
Outlook	Stable

REPORT CONTENTS

DECEMBER 2017

HABIB CONSTRUCTION SERVICES (PUBLIC) LIMITED (HCS) PROFILE	
Incorporated	2009
Major Business	Construction
Legal Status	Un-Listed
Head Office	Lahore

INDUSTRY SNAPSHOT

Construction sector's share in GDP was 2.74% in FY17 against a share of 2.65% last year. This sector has witnessed a growth of 9.05% against a growth of 14.6% last year, as many CPEC related projects were initiated in 2015-16. Of these projects, only a few handful of companies have benefitted most as they enjoy economy of scales, good relationship with government bodies and can bid the lowest price. Most of the companies secure contracts based on their branding within the industry, word of mouth, and their ability to execute.

OWNERSHIP — GOOD

- HCS is registered as a public limited company with 29 shareholders. Five shareholders own 74.4% of the shares while the rest are held by the management team.
- Mr Shahid Saleem, CEO, with 51% ownership and one of the founding members of HCS, has over 30 years of experience in various appointments in renowned private sector construction companies. He is the person behind the success of the company leading with his visionary leadership.

GOVERNANCE — ADEQUATE

- The overall control of the company vests in the seven-member board of directors. Five are executive directors, while one is an independent director and the other is a member of the sponsoring family.
- Although the presence of an independent director is important to ensure effective, transparent and independent oversight, the company would do better if it had its own internal audit function.
- The auditors of the company M/S Tariq Abdul Ghani Maqbool & Co. Chartered Accountants issued an unqualified audit opinion pertaining to annual financial statements for FY17.

MANAGEMENT — GOOD

- HCS has a lean organizational structure with an experienced management team; a balanced mix of professionals from the construction industry.
- Mr. Shahid Saleem is the CEO and is assisted by a team of experienced professionals.
- Mr M. Azam Bhatti, Chairman of the Board, is a professional engineer and has 41 years of experience both in the Army as well as in the private sector. Mr Muhammad Shabir is a graduate in Quantity Surveying from UK and has worked in Quantity Surveying Consultancy in UK and upon returning to Pakistan has worked with NLC and NHA in various capacities. Mr Mohsin Hussnain is a fellow member of ICAP and IFPA. He has over 15 years of experience while serving in senior positions in renowned private sector companies. Ms Afia Suhail, holds a BSc in Civil Engineering and Masters in Environmental Design and has worked in senior positions in well-known consultancy's in Pakistan and abroad. General (retired) Ziauddin, independent director, is BSc Engineer from Military College of Engineering and has vast experience of large civil engineering projects. Ms Kainat Shahid, CEO's daughter, has a BSc Economics from LUMS and a Masters in Finance from University of Warwick.

SYSTEMS & CONTROLS — GOOD

- HCS is currently using an ERP software customized for the construction industry from E-Tech.
- The software keeps track of receivables, payables, general ledger, accounts, etc. The payables module further bifurcates into GL based payables and un-invoiced payables, as unique to construction industry, materials are continuously arriving at project sites and at times even before a formal invoice is received by the company. To keep track of this movement in payables, this customization has been done so that management is always cognizant of its liabilities.
- The company's MIS generates quarterly reports for the Board. Whereas the project management module is used on a daily basis which keeps track of all the elements related to specific projects.

PERFORMANCE — GOOD

- During FY17, the entity's revenues witnessed a slight drop of 9.2% in comparison to prior year growth of 95.3% (FY17: PKR 17.916bln; FY16: PKR 19.729bln).
- During FY17, though topline dropped a little, a slight increase in the cost of sales slightly decreased gross margins (FY17: 16.6%, FY16: 17.2%) primarily due to increase in salaries and wages.
- With a slightly decreasing gross margin, but a considerably lower finance cost (FY17: 91mln, FY16: 171mln), however, resulted in growth of net profit margin for the period (FY17: 8.1%, FY16: 7.6%).
- HCS has some major projects in the pipeline starting in a few months' time. The entity is looking at contracts in excess of PKR 60 billion from infrastructure related construction projects in the next two years.

FINANCIAL RISK — GOOD

- Although net working capital days have increased a little, (FY17: 31 days, FY16: 21 days), they are still considerably good compared to the industry. As at end FY17, working capital requirements of the company increased primarily due to increase in trade payables.
- During FY17, HCS STBs were slashed by PKR 3.2bln resulting in short-term total leverage of the company (room to borrow) increasing to 42% (FY16: 17%).
- In FY17, HCS's operating cashflows (FCFO) dropped to PKR 1.68bln (FY16: 1.97bln) due to lesser revenue compared from last year.
- Due to a monumental decrease in short term borrowing, interest coverage ratio improved considerably (FY17: 18.5x, FY16: 11.5x). The company has not procured long term debt so far and has been funding the business through its equity, so going forward, if circumstances demand HCS has enough room to procure debt to further fuel its already robust growth.

PKR mln

Habib Construction Services (Public) Limited

BALANCE SHEET	30-Jun-17	30-Jun-16	30-Jun-15
	Annual	Annual	Annual
Non-Current Assets	**3,345**	**2,358**	**1,236**
Investments (Incl. Associates)	**7**	**-**	**24**
Equity	7	-	24
Debt Securities	-	-	-
Current Assets	**8,101**	**12,357**	**3,809**
Inventory	411	726	102
Trade Receivables	2,559	2,385	1,445
Others	5,131	9,246	2,262
Total Assets	**11,453**	**14,715**	**5,068**
Debt	**153**	**3,379**	**-**
Short-Term	153	3,379	-
Long-term (Incl. Current Maturity of Long-Term Debt)	-	-	-
Other Short-Term Liabilities	4,580	6,882	2,337
Other Long-Term Liabilities	16	12	9
Shareholder's Equity	**6,704**	**4,442**	**2,722**
Total Liabilities & Equity	**11,453**	**14,715**	**5,068**
INCOME STATEMENT			
Turnover	**17,916**	**19,729**	**10,102**
Gross Profit	2,972	3,386	1,550
Other Income	50	(11)	6
Financial Charges	(91)	(171)	(22)
Net Income	**1,459**	**1,507**	**728**
Cashflow Statement			
EBITDA	2,988	3,404	1,575
Free Cashflow from Operations (FCFO)	1,685	1,971	903
Net Cash changes in Working Capital	1,518	(4,842)	(750)
Net Cash from Operating Activities	3,112	(3,042)	132
Net Cash from InvestingActivities	(360)	(1,017)	(310)
Net Cash from Financing Activities	(3,379)	3,379	(200)
Net Cash Generated during the period	(627)	(680)	(378)
Ratio Analysis			
Performance			
Turnover Growth (same period last year)	-9.2%	95.3%	49.3%
Gross Margin	16.6%	17.2%	15.3%
Net Margin	8.1%	7.6%	7.2%
ROE	26.2%	42.1%	29.6%
Coverages			
Debt Service Coverage (x) (FCFO/Gross Interest+CMLTD+Uncc	18.5	11.5	22.3
Interest Coverage (x) (FCFO/Gross Interest)	18.5	11.5	22.3
Debt Payback (Years) (Total Lt.Debt (excluding Covered Short T	0.0	0.0	0.0
Liquidity			
Net Cash Cycle (Inventory Days + Receivable Days - Payable Day	31	21	27
Capital Structure (Total Debt/Total Debt+Equity)	2%	43%	0%

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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Rated Entity	
Name of Rated Entity	Habib Construction Services Public Limited
Sector	Construction
Type of Relationship	Solicited
Purpose of the Rating	Independent Risk Assessment

Rating History

Entity

Dissemination Date	Long Term	Short Term	Outlook	Action
29-Dec-17	A-	A2	Stable	Initial

Related Criteria and Research: Construction Sector | Dec-17

Methodology: Corporate Rating Methodology|Jul17

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Rating Team Statement

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