



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
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	-
23-Jun-2017	A-	A1	Stable	Initial	-

#### Rating Rationale and Key Rating Drivers

EFG Hermes Pakistan Limited ('EFGH' or the 'Company') has the backing of a seasoned financial services group "EFG Hermes". The group has a presence across fourteen countries spanning four continents across the globe. EFGH primarily offers equity brokerage and research services, while MFS/MTS are also present. To cover its finance cost and augment the bottom line, the Company invests all excess funds into low-risk market T-bills. Rising interest rates, political uncertainty, and increasing inflationary pressure during CY22 have impeded investors' sentiments, adversely impacting volumetric activity at PSX. To address the volumetric decline, the Company shifted its focus towards retail clients, and as a result sustained its market share during 9MCY22. EFGH's revenue fell by ~48% during 9MCY22 to ~PKR 94mln (SPLY: ~PKR 181mln) while market volumes declined by ~57% during the same period. The profitability remained under stress, with the Company suffering from a loss after tax of ~PKR 68mln during 9MCY22. The assigned ratings incorporate the continued financial support of the sponsor through guaranteed loan facilities of PKR 825mln. During the 9MCY22, the sponsor reclassified its inter-company receivable, enhancing EFGH's equity base by ~PKR 118mln. The Company's equity has declined over the years due to losses, standing at ~PKR 207mln at end-Sep'22, and may be improved through further equity injections. Going forward, EFGH plans to further penetrate the retail clientele by enhancing its online presence by launching a customized mobile application. The recent volatility in trading volumes has heightened the exposure to business risk while going forward, capital market activity is expected to remain subdued amidst high inflation and interest rate environment. EFGH's revenue is concentrated in equity brokerage, and revenue diversification is required in the prevailing market conditions. The assigned ratings draw comfort from the strong governance and control framework of the Company. EFGH does not engage in proprietary book investments, thus limiting market risk.

The ratings depend on the management's ability to retain its market share and enhance the volumes and diversity of revenue to improve its competitive position in the brokerage industry. Retention of key personnel and profitability sustainability will remain imperative from a rating perspective.

#### 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   Correlation Between Long-term & Short-term Rating Scales(Jun-22),Methodology   Rating Modifiers(Jun-22),Methodology   Broker Entity Rating(Jun-22)
<b>Related Research</b>	Sector Study   Brokerage & Securities(Jan-22)
<b>Rating Analysts</b>	Afnan Iqbal   afnan.iqbal@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 ~\$53mln profit during 9MCY22, while its equity stood at ~\$787mln at end-Sep'22.

### 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 CY21. 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** Pakistan's economy during CY22 has remained largely volatile. From international aspects such as the global recession and the Russia-Ukraine war to domestic political uncertainty and flash floods devastating a significant part of the country, investors have had no confidence in the market. Traded volumes have remained low which has affected the top line of the brokerage industry as a whole. Political stability after elections may play a significant factor in possibly stabilizing the market; however, the recent increase in policy interest rates may continue to deter investors towards safer fixed-income returns instead of the riskier equity market.

**Relative Position** Despite a decline in market volumes, EFGH has managed to sustain its market share during 9MCY22.

**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 9MCY22, the brokerage commission stood at ~PKR 94mln while during 9MCY21 it stood at ~PKR 181 mln (CY21: ~PKR 241.6 mln). The decrease in the topline is due to declining in market volumes in 9MCY22 when compared with 9MCY21. The market volumes declined by ~57% whereas EFGH's revenue declined by ~48% during 9MCY22 when compared with 9MCY21.

**Cost Structure** The Company's operating and administrative expenses stood at ~PKR 144mln during 9MCY22 (SPLY: ~PKR 138mln). An increase in the amount of debt combined with the increase in market interest rates, resulted in EFGH's finance cost increasing to ~PKR 78mln (SPLY: ~PKR 27mln). As a result of the decline in the top line and surge in finance cost, the Company reported a net loss of ~PKR 68mln during 9MCY22 as compared to a profit of ~PKR 30mln during 9MCY21.

**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 1,251mln at end-Sep'22 as compared to current liabilities of ~PKR 272mln. 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. During the quarter that ended Sep'22, the parent company reclassified its inter-company receivable balance, increasing the equity of EFGH by ~PKR 118mln, and as a result, the equity of EFGH stands at ~PKR 207mln at end-Sep'22.



PKR mln

EFG Hermes Pakistan Limited  
Listed Public Limited

Sep-22	Dec-21	Dec-20	Dec-19
9M	12M	12M	12M

#### A BALANCE SHEET

1 Finances	88	80	41	13
2 Investments	911	841	416	396
3 Other Earning Assets	11	11	11	11
4 Non-Earning Assets	293	385	394	341
5 Non-Performing Finances-net	-	-	-	-
<b>Total Assets</b>	<b>1,304</b>	<b>1,317</b>	<b>862</b>	<b>762</b>
6 Funding	873	825	440	447
7 Other Liabilities (Non-Interest Bearing)	224	329	286	184
<b>Total Liabilities</b>	<b>1,097</b>	<b>1,154</b>	<b>726</b>	<b>631</b>
<b>Equity</b>	<b>207</b>	<b>163</b>	<b>136</b>	<b>131</b>

#### B INCOME STATEMENT

1 Fee Based Income	93	242	172	123
2 Operating Expenses	(144)	(196)	(158)	(167)
3 Non Fee Based Income	74	45	43	51
<b>Total Operating Income/(Loss)</b>	<b>23</b>	<b>90</b>	<b>57</b>	<b>8</b>
4 Financial Charges	(78)	(44)	(40)	(45)
<b>Pre-Tax Profit</b>	<b>(55)</b>	<b>47</b>	<b>16</b>	<b>(37)</b>
5 Taxes	(12)	(18)	(15)	(11)
<b>Profit After Tax</b>	<b>(68)</b>	<b>29</b>	<b>2</b>	<b>(48)</b>

#### C RATIO ANALYSIS

##### 1 Cost Structure

Financial Charges / Total Operating Income/(Loss)	344.2%	48.4%	71.4%	571.7%
Return on Equity (ROE)	-78.1%	25.4%	1.6%	-45.3%

##### 2 Capital Adequacy

Equity / Total Assets (D+E+F)	15.9%	12.4%	15.8%	17.1%
Free Cash Flows from Operations (FCFO) / (Financial Charges + Current Maturity of Long Term Debt + Uncovered Short Term Borrowings)	4.9%	187.8%	15.3%	-82.5%

##### 3 Liquidity

Liquid Assets / Total Assets (D+E+F)	79.5%	76.0%	69.3%	66.0%
Liquid Assets / Trade Related Liabilities	485.9%	583.0%	217.6%	291.0%

##### 4 Credit & Market Risk

Accounts Receivable / Short-term Borrowings + Advances from Customers + Payables to Customers	3.7%	6.3%	2.7%	8.8%
Equity Instruments / Investments	2.6%	3.6%	7.6%	7.1%

### 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+	<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	
BBB-	
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	
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	<b>Very high credit risk.</b> Substantial credit risk "CCC" Default is a real possibility.
CC	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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### **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 | 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)

(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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