The Pakistan Credit Rating Agency Limited

PAKISTAN MOBILE COMMUNICATIONS LIMITED

	NEW [NOV-17]	PREVIOUS [MAR-17]
Sukuk	AA	AA
Outlook	Positive	Positive
Rating Watch	-	-

REPORT CONTENTS

NOVEMBER 2017

Profile &Ownership

- Pakistan Mobile Communications Limited (PMCL) is the largest cellular telecommunication service provider in Pakistan. As at end-Aug17, its market share in terms of cellular subscriptions is of 38%.
- In November, 2015 VEON (Previously: Vimpelcom) and Abu Dhabi Group have signed an agreement to merge their telecom subsidiaries in Pakistan. Resultantly, Jazz (Mobilink) and Warid effectively merged in July-16.
- PMCL under the new brand name Jazz is providing all its cellular services including 3G, 4G and LTE.
- The ultimate sponsors of the company are VEON (Previously: Vimpelcom) with ~85% indirect holding in PMCL via 51% holding in Global Telecom Holdings.

Governance

- The seven-member Board of Directors (BoD) is mainly composed of representatives from VEON.
- The Board is chaired by His Highness Sheikh Nahayan Mabarak Al Nahayan. He heads the United Arab Emirates Ministry of Culture, Youth, and Social Development. He also chairs the board of the Abu Dhabi Group, Union National Bank, Bank Alfalah and United Bank Limited.
- The board comprises of three executive directors comprising CEO, CFO and the company secretary.
- The board comprises highly qualified and experienced professionals holding senior positions in group companies.

Management

- PMCL has an experienced top management team with requisite background and qualification. They are equipped with both local and foreign experience.
- Mr. Aamir Ibrahim – Ex CCO of PMCL has been appointed as CEO of merged entity in July 16. He has over two decades experience of blue chip companies across various countries and industries but majorly of telecom sector.

Business Risk

- With the regain of subscriber base in CY16, PMCL's top-line on standalone basis exhibited an increasing trend (Dec16: PKR 122,696mln; Dec15: PKR 94,300mln; Dec14: PKR 92,379mln) attributable to growth in data ARPUs.
- Merged entity topline stayed at PKR 128,751mln giving an increase of 29% on YoY basis, however, in 1HCY17 with an increase of 34% revenue of PKR 74,599mln (1HCY16: PKR 55,702mln) was achieved.
- Post-merger administrative expenses increased by 32% (Dec16: PKR 32,512mln; Dec15: PKR 24,677mln), however, financial expenses exhibited a marginal increase (Dec16: PKR 4,672mln; Dec15: PKR 4,538mln).
- Increased gross margins helped absorbing increased admin and tax expenses generating profit of PKR 10,210mln (Dec15: Loss of PKR 1,223mln).
- During 1HCY17, increased topline along with other income majorly on account of site sharing revenue helped company absorbing its increased tax expenses and also to rest at bottom line of PKR 7,641mln (1HCY16: PKR 2,374).
- The said merger brought synergies of more than USD115mln.
- During CY16, PMCL managed to acquire 10MHZ of 1800MHZ 4G/LTE spectrum with an investment of USD 295mln. Also in late August17, PMCL managed to sale its 13,000 towers through sale of its wholly owned subsidiary Deodar (Pvt.) to Edotco (a Malaysian based company).
- Going forward, the company is eyeing to keep its market share intact while grabbing the diversified business opportunities.

Financial Risk

- The company maintains reasonably good cash conversion ratio; increased considerably YoY (FCFO adjusted for WC/sales Jun17: 30%; Dec16: 43%; Dec15: 27%) due to efficient working capital management.
- FCFO of the company witnessed decent improvement (Jun17: PKR 25,552; Dec16: PKR 45,243mln; Dec15: PKR 38,753mln) owing to higher EBITDA; resultantly improvement in coverages was observed YoY (FCFO/Gross Interest Jun17: 10x; Dec16: 8.1x; Dec15: 7.2x).
- The company net cash cycle days exhibited decreasing trend (Jun17: -15days; Dec16: -8days, Dec15: 1days) owing to increased creditor days.
- Post-merger PMCL's capital structure remained moderately leveraged (Debt/Debt+Equity: Jun17: 54.6%; Dec16: 51.2%; Dec15: 52.1%).
- The company has issued a Sukuk of PKR 6,900mln completely disbursed in Sep-15 and expected to mature in Dec-19.

RATING RATIONALE AND KEY RATING DRIVERS

Pakistan Mobile Communications Limited (PMCL) – majority owned by Veon (VimpelCom) is the largest cellular operator in Pakistan. After acquiring Warid Telecom (an Abu Dhabi Group company with ~11mln subscribers at end FY16) in July16, PMCL now commands 38% market share (51mln subscribers at end-Jan17). The said merger while giving significant volumes, brought operational and technical network related synergies that are reflected in significantly better EBITDA and profitability of merged entity. PMCL commissioned marketing, technical, distribution and human resource integration in an efficient manner. A significant progress has been achieved. Post-merger, PMCL has consolidated all its products and services under single brand 'Jazz'.

PMCL enjoys strong volumes and profitability; which gives it a strong business profile. Erstwhile Warid had relatively squeezed margins - an opportunity for PMCL. PMCL improved EBITDA margins above 40% in 1HCY17. The merger brought sizeable debt. However, the overall debt profile stays robust (EBITDA total debt payback = less than 3 years). Going forward, PMCL, while eying volume growth, is focusing on achieving better penetration in to existing base. Data services and mobile financial services are its key focus. The company marked a step in asset light operating model; sale of Deodar wholly owned subsidiary with tower business to EdotCo (Malaysian based Company). This while freeing up financial sources, would enable focus towards core and differentiating services. PMCL, using the platform of Mobilink Microfinance Bank, an associate entity, intends to establish a strong digital banking platform. All these should enable PMCL to uphold its position in the competitive landscape. Launch of VEON app; is another step to capitalise data market industry of Pakistan.

The Positive Outlook is maintained which recognize i) strengthening market positioning, ii) likely synergy gains in EBITDA and profitability margins; iii) adequate debt profile; iv) synergizing technological and distributional channels and v) potential of Jazz cash. Meanwhile, diversifying revenue channels while maintaining performance matrix would be improved.

INDUSTRY

- Competitive landscape of the industry with four cellular players.
- Revitalization towards data communication and mobile banking
- Low pricing creating pressure on industry EBITDA margins.
- On the brink of technology future growth of industry will increase revenues and efficiencies to the whole economy.

Pakistan Mobile Communications Limited — PKR mln

BALANCE SHEET	30-Jun-17	30-Dec-16	31-Dec-15	31-Dec-15	31-Dec-14
	1HCY17(Cons.)	CY16 (Cons.)	CY15 (Cons.)	CY15	CY14
Non-Current Assets	**205,948**	**215,286**	**128,851**	**124,898**	**137,047**
Investments (Others)	-	-	-	**5,565**	**5,301**
Current Assets	**56,701**	**30,891**	**13,954**	**8,773**	**11,553**
Inventory (Finished Goods)	471	234	433	433	222
Trade Receivables	6,908	6,399	3,412	2,204	1,980
Other Current Assets	42,852	7,919	7,252	4,056	3,821
Cash & Bank Balances	6,470	16,338	2,857	2,081	5,530
Total Assets	**262,649**	**246,176**	**142,805**	**139,236**	**153,901**
Debt	**93,650**	**77,266**	**45,098**	**44,627**	**40,875**
Short-term	-	-	-	-	-
Long-term (Inlc. Current Maturity of long-term debt)	**93,650**	**77,266**	**45,098**	**44,627**	**40,875**
Trade Payables	8,856	7,321	2,773	6,029	20,672
Due to Associates	-	-	-	609	136
Provision for Taxation	1,058	3,642	6,263	4,486	4,943
Other Liabilities	71,116	72,683	47,172	51,801	52,331
Shareholder's Equity	**84,435**	**80,264**	**41,499**	**31,684**	**34,944**
Total Liabilities & Equity	**259,115**	**241,176**	**142,805**	**139,236**	**153,901**

INCOME STATEMENT					
Turnover	**74,599**	**128,751**	**99,912**	**94,300**	**92,379**
Gross Profit	29,578	49,673	25,266	22,525	28,029
Operating Profit	14,129	17,162	589	(1,481)	7,193
Other Income	621	788	543	3,489	3,138
Financial Charges	(2,125)	(4,672)	(4,538)	(4,562)	(4,473)
Taxation	(7,600)	(7,136)	19	784	(8,957)
Net Income	**7,641**	**10,210**	**(1,223)**	**(2,703)**	**(1,438)**

Cashflow Statement					
Free Cashflow from Operations (FCFO)	25,552	45,243	38,753	36,896	32,760
Net Cash changes in Working Capital	(3,147)	10,305	(12,104)	(14,983)	10,758
Net Cash from Operating Activities	21,133	52,808	23,148	17,849	40,269
Net Cash from InvestingActivities	(43,074)	(23,705)	(24,997)	(23,854)	(67,840)
Net Cash from Financing Activities	12,742	(17,086)	(1,164)	3,336	20,681
Net Cash generated during the period	(9,198)	12,017	(3,014)	(2,669)	(6,891)
Closing Balance of Cash & Equivalents	6,770	16,338	3,637	2,860	5,530

Ratio Analysis					
Performance					
Turnover Growth	42.3%	28.9%	8.2%	34.7%	21.8%
Gross Margin	39.7%	38.6%	25.3%	23.9%	30.3%
EBITDA Margin	44.0%	39.1%	41.9%	41.3%	40.1%
Net Margin	10.2%	7.9%	-1.2%	-2.9%	-1.6%
ROE	13.4%	10.0%	-2.3%	-6.4%	-3.2%
Coverages					
Debt Service Coverage					
1. (FCFO/Gross Interest+CMLTD) (X)	1.8	1.8	2.1	2.1	2.5
2. (FCFO/Gross Interest+CMLTD+Uncovered STB) (X)	1.1	0.6	0.7	0.6	2.5
Interest Coverage					
1. (FCFO/Gross Interest) (X)	10.1	8.1	7.2	6.8	7.3
2. (EBITDA/Gross Interest) (X)	13.0	9.0	7.7	7.2	8.3
Liquidity and Cashflows					
Current ratio excluding CMLTD (X)	0.7	0.4	0.3	0.2	0.2
Net Cash Cycle (Inventory Days + Receivable Days - Payable	-15.1	-9.1	-21.3	-43.4	-120.0
Capital Structure (Total Debt/Total Debt+Equity)	54.6%	51.2%	52.1%	58.5%	53.9%

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

Rating	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 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