



The Pakistan Credit Rating Agency Limited

**Rating Report**

**Honda Centre (Pvt.) Limited**

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Rating History					
Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
	BBB	A3	Stable	Initial	-

**Rating Rationale and Key Rating Drivers**

Car dealership (authorized) rides on the strength of the Principal (auto manufacturer/assembler). The stronger the Principal in the respective market, higher is the standing of the car dealer. There is a pre-defined set of criteria – qualitative & quantitative – that the Principal demands of the dealer network. The rating takes comfort from Honda Centres' alliance to Honda Atlas Cars Pakistan Limited– owned by Atlas Group and Honda Motor Company Limited, Japan. Honda Centre is one of the largest authorized 3S dealership for Honda Atlas Cars Pakistan Limited in Pakistan. Honda Centre (Pvt) Limited (HC) has been in the auto dealership industry for over a decade now. The sponsors have a good understanding of the business. The company's profitability and leveraging is good. The sponsors have injected a sizeable amount as subordinated debt. The overall auto sector business is dependent on economic indicators and demand led by businesses and investors. Honda Centre has built a sustainable position in the competitive auto industry of Pakistan. The volumes are rising. Honda Centre has captured adequate market share over a decade of operations. It is important to sustain the growth while managing the rising competition, which is more of a Principal's domain. Foreign players are also taking interest in the local market. Control environment may be strengthened by including independent directorship and adopting quarterly accounts.

The ratings are dependent on sustaining a steady revenue stream and financial risk profile. Any prolonged downturn in subdued business volume can have a detrimental effect on the rating. Good corporate governance practice is considered pivotal for a growing business concern.

Disclosure	
<b>Name of Rated Entity</b>	Honda Centre (Pvt.) Limited
<b>Type of Relationship</b>	Solicited
<b>Purpose of the Rating</b>	Entity Rating
<b>Applicable Criteria</b>	Methodology   Corporate Rating Methodology(27-Jul-17)
<b>Related Research</b>	Sector Study   Auto and Allied   Passenger Cars(23-Feb-18)
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HONDA CENTRE (PRIVATE) LIMITED (HC) PROFILE	
<b>Incorporated</b>	2007
<b>Major Business</b>	Auto Dealership
<b>Legal Status</b>	Un-Listed
<b>Head Office</b>	Rawalpindi

INDUSTRY SNAPSHOT
Automobile sector is amongst the top growth sectors in the large scale manufacturing in Pakistan. The sector has shown robust growth in the past many years (FY17: 11%, FY16: 23%) primarily due to historically low interest rates, coupled with improving macro-economic indicators which have led to higher consumer financing especially auto financing.

OWNERSHIP	GOOD
<ul style="list-style-type: none"> <li>HC is registered as a private limited company. The three shareholders, who are brothers, each own 33% stake in the company.</li> <li>The eldest brother, Mr. Yasir Raza is the Chief Executive Officer, who holds a Bachelor's degree from UET and an MBA from London Metropolitan University, carries years of experience in the technology and oil &amp; gas sectors. Dr. Taimur Raza, CEO's younger brother, holds an MBBS from Hamdard University and an MRCP degree from the UK. He has previously worked as a medical professional and is now part of the HC team. Mr. Hassan Raza, executive director, and youngest amongst the three directors holds a BA and MBA degrees from Indiana University. He has worked extensively in the consultancy sector internationally, with prestigious firms like KPMG in the UK, and Deloitte and EY in USA.</li> </ul>	

GOVERNANCE	ADEQUATE
<ul style="list-style-type: none"> <li>The overall control of the company vests in three-member board of directors (BoD).</li> <li>To ensure effective, transparent and independent oversight of the company internal audit function plays a pivotal role which could report directly to the Board.</li> <li>M/s. Horwath Hussain Chaudhury &amp; Co. Chartered Accountants, is the external auditor of the company. The auditors have expressed an unqualified audit opinion on the financial statements of Honda Centre for the year ended June 30, 2017.</li> </ul>	

MANAGEMENT	GOOD
<ul style="list-style-type: none"> <li>HC has a lean organizational structure with an experienced management team and a balanced mix of professionals.</li> <li>The three executive directors have been associated with the Board for the past 11 years, each having a minimum experience of 18 years in different sectors bringing a breadth of multi-faceted experience to the Company.</li> <li>Mr. Yasir Raza, CEO, besides the general oversight looks after the technical side of the business. Mr. Taimur Raza heads the Finance department while Mr. Hassan Raza look after the business development and sales function of Honda Centre. The top Management includes four key professionals. Mr. Ali Sher Khan, Sr. Manager Sales &amp; Marketing, holds a BS from USA and has been associated with HC for the past 3 years. Mr. Zeeshan Ali, Sr. Manager Sales &amp; Operations, is an MBA, and has been associated with HC for the past 9 years. Ms. Farzana Ahmed, General Manager HR &amp; Operations has been associated with HC for 6 years and Mr. Muhammad Bin Qasim, CFO, is a chartered accountant and has been with HC for 4 years.</li> </ul>	

SYSTEMS & CONTROLS	GOOD
<ul style="list-style-type: none"> <li>HC is currently using Microsoft's enterprise resource planning software, Dynamics AX 2012.</li> <li>The functionality of this software includes warehouse and transport management, budget planning, demand forecasting, human resources and point of sale. The software provides comprehensive core functionality – financials, human resources, and operations management – to run efficiently, make smart business decisions, and engage with a diverse array of customers.</li> <li>The company's MIS generates Balance Sheet, Profit and Loss, and Cash flow statements on a weekly basis for the Board. The MIS generated Sales reports are reviewed by the top management on a daily basis.</li> </ul>	

PERFORMANCE	GOOD
<ul style="list-style-type: none"> <li>During FY17, the entity's revenues witnessed a sharp increase of 10% in comparison to prior year growth of 2% (FY17: PKR 285mln; FY16: PKR 260mln).</li> <li>During FY17, although topline increased, a slight increase in the operating expenses slightly decreased operating margin (FY17: 65%, FY16: 66%) primarily due to increase in depreciation expenses.</li> <li>With a slightly decreasing gross margin, but a considerably higher non-recurring non-core income from revaluation of fixed assets (FY17: 18mln, FY16: 10mln), however, resulted in growth of net profit margin for the period (FY17: 43%, FY16: 41%).</li> </ul>	

FINANCIAL RISK	GOOD
<ul style="list-style-type: none"> <li>Although net working capital days have decreased significantly, (FY17: 291 days, FY16: 324 days), they are still slightly on the higher side. As at end FY17, short term borrowing of the company were stagnant (FY17: 324mln, FY16: 325mln) which were being used for working capital management.</li> <li>In FY17, HC's operating cashflows (FCFO) increased to PKR 166mln (FY16: 146mln) due to higher revenue compared from last year.</li> <li>As short term borrowing were at the same level as last year (FY17: 324mln, FY16: 325mln), interest coverage ratio stood constant at 5.9x. Debt coverage ratio on the other hand dropped (FY17: 4.3x, FY16: 5.8x) primarily due to servicing of higher finance lease payments.</li> <li>At end-FY17, the company had a slightly levered capital structure, with a debt to debt plus equity ratio of 56% (FY16: 64%). Although Long Term Debt increased up to PKR 258mln (FY16: 235mln), 90% (234mln) of this LTD is a loan obtained from directors without markup and security.</li> </ul>	



## Honda Centre (Private) Ltd

BALANCE SHEET	30-Jun-17	30-Jun-16	30-Jun-15
	CY17	CY16	CY15
<b>Non-Current Assets</b>	<b>627</b>	<b>463</b>	<b>468</b>
<b>Investments (Incl. Associates)</b>	-	-	-
Equity	-	-	-
Debt	-	-	-
<b>Current Assets</b>	<b>472</b>	<b>476</b>	<b>515</b>
Inventory	93	90	122
Trade Receivables	130	139	110
Others	249	246	283
<b>Total Assets</b>	<b>1,099</b>	<b>939</b>	<b>983</b>
<b>Debt</b>	<b>334</b>	<b>325</b>	<b>274</b>
Short-term	324	325	274
Long-term (Incl. Current Maturity of Long-Term Debt)	10	1	-
Other Short-term Liabilities	63	60	60
Other Long-term Liabilities	248	234	230
<b>Shareholder's Equity</b>	<b>454</b>	<b>320</b>	<b>418</b>
<b>Total Liabilities &amp; Equity</b>	<b>1,099</b>	<b>939</b>	<b>983</b>
<b>INCOME STATEMENT</b>			
<b>Turnover</b>	<b>286</b>	<b>260</b>	<b>255</b>
Gross Profit	286	260	255
Other Income	18	10	4
Financial Charges	(28)	(25)	(22)
<b>Net Income</b>	<b>122</b>	<b>107</b>	<b>97</b>
<b>Cashflow Statement</b>			
Free Cashflow from Operations (FCFO)	166	146	124
Net Cash changes in Working Capital	6	52	(135)
Net Cash from Operating Activities	146	173	(11)
Net Cash from Investing Activities	(11)	(8)	(26)
Net Cash from Financing Activities	(135)	(156)	39
Net Cash generated during the period	(0)	9	2
<b>Ratio Analysis</b>			
<b>Performance</b>			
Turnover Growth	9.9%	2.1%	17.6%
Gross Margin	100.0%	100.0%	100.0%
Net Margin	42.6%	41.2%	38.0%
ROE	18.8%	22.0%	23.1%
<b>Coverages</b>			
Debt Service Coverage (x) (FCFO/Gross Interest+CMLTD+Uncovered)	4.3	5.8	5.6
Interest Coverage (x) (FCFO/Gross Interest)	5.9	5.9	5.6
Debt Payback (Years) (Total Lt.Debt (excluding Covered Short Term B.	1.9	1.9	2.3
<b>Liquidity</b>			
Net Cash Cycle (Inventory Days + Receivable Days - Payable Days)	291.2	323.6	330.2
<b>Capital Structure</b> (Total Debt/Total Debt+Equity)	56.1%	63.6%	54.7%

## 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.

<b>LONG TERM RATINGS</b>		<b>SHORT TERM RATINGS</b>
<b>AAA</b>	<b>Highest credit quality.</b> Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments.	<p><b>A1+:</b> The highest capacity for timely repayment.</p> <p><b>A1:</b> A strong capacity for timely repayment.</p> <p><b>A2:</b> A satisfactory capacity for timely repayment. This may be susceptible to adverse changes in business, economic, or financial conditions.</p> <p><b>A3:</b> An adequate capacity for timely repayment. Such capacity is susceptible to adverse changes in business, economic, or financial conditions.</p> <p><b>B:</b> The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions.</p> <p><b>C:</b> An inadequate capacity to ensure timely repayment.</p>
<b>AA+</b>	<b>Very high credit quality.</b> Very low expectation of credit risk.	
<b>AA</b>	Indicate very strong capacity for timely payment of financial commitments. This capacity is not significantly vulnerable to foreseeable events.	
<b>AA-</b>		
<b>A+</b>	<b>High credit quality.</b> Low expectation of credit risk.	
<b>A</b>	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.	
<b>A-</b>		
<b>BBB+</b>	<b>Good credit quality.</b> Currently a low expectation of credit risk.	
<b>BBB</b>	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.	
<b>BBB-</b>		
<b>BB+</b>	<b>Moderate risk.</b> Possibility of credit risk developing.	
<b>BB</b>	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>BB-</b>		
<b>B+</b>	<b>High credit risk.</b>	
<b>B</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>B-</b>		
<b>CCC</b>	<b>Very high credit risk.</b> Substantial credit risk	
<b>CC</b>	“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.	
<b>C</b>		
<b>D</b>	Obligations are currently in default.	

<p><b>Outlook (Stable, Positive, Negative, Developing)</b> 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’.</p>	<p><b>Rating Watch</b> 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.</p>	<p><b>Suspension</b> 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.</p>	<p><b>Withdrawn</b> 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 surveil the opinion due to lack of requisite information</p>
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(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)

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- 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

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- (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.
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- (10) PACRA maintains principal of integrity in seeking rating business | Chapter III; 11-A-(u)
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- (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)

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(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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