



The Pakistan Credit Rating Agency Limited

Rating Report

Airlink Communication

Report Contents

1. Rating Analysis
2. Financial Information
3. Rating Scale
4. Regulatory and Supplementary Disclosure

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
27-Dec-2019	A-	A1	Stable	Maintain	-
28-Jun-2019	A-	A1	Stable	Maintain	YES
31-Dec-2018	A-	A1	Stable	Upgrade	-
10-Jul-2018	BBB+	A2	Stable	Maintain	-
29-Dec-2017	BBB+	A2	Stable	Initial	-

Rating Rationale and Key Rating Drivers

The ratings denote Airlink's adequate operational sustainability underpinned by its solid market position and diversified earnings from its mobile distribution business. Over the last few years, the Company has improved its business profile. Topline is witnessing an ample growth on a Year-on-Year basis owing to the formidable demand of mobile handsets in the country. Recent global tension among Huawei and USA were expected to hamper the business volumes of the country. However, Airlink has been successful in subduing the challenge by replacing the foregone Huawei offtake with the sales of a new brand - Tecno. Additionally, the Company has also been awarded the distribution rights of Apple phones in the country, in collaboration with a Singaporean Group. This is also expected to nurture the topline. With its legal status converted to a Public Listed Entity in Apr'19, several improvements in the governance structure are witnessed including induction of three independent directors. Move is on the horizon for public listing. The company's import driven business model is mandated to be secured against cash margin with insurance for the in-transit; short term debt book, therefore, appears ballooned on account of regulatory compliance of import contracts - effective working capital strategies are imperative. Financial risk profile is demonstrated by sanguine free cash flows from operations (FCFO) and leveraged capital structure.

The ratings are dependent on the company's ability to sustain its relative position and positive performance indicators amidst growth. As business volumes grow, prudent financial discipline - particularly in capital structure, is essential to uphold the ratings.

Disclosure

Name of Rated Entity	Airlink Communication
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology Corporate Ratings(Jun-19),Methodology Correlation Between Long-Term And Short-Term Rating Scale(Jun-19),Criteria Rating Modifier(Jun-19)
Related Research	Sector Study Mobile Phone and Allied Products(Jun-19)
Rating Analysts	Mubashir Nazir mubashir.nazir@pacra.com +92-42-35869504

Profile

Legal Structure Airlink Communication Limited (herein referred to as "Airlink" or "the company") is a Public Unlisted Company that was incorporated as a Private Limited Company in 2014 with the SECP under Companies Ordinance, 1984 (now Companies Act, 2017). Airlink converted its status to Public Unlisted in Apr'19.

Background Airlink was formed in 2010 as a partnership firm for the import and distribution of IT products, particularly mobile phones, and related services. In 2014, a new private company was incorporated simultaneously to take over the business of the partnership firm running as a family business. Following July 2018, the entire business of the partnership has been transferred to the company's books.

Operations Airlink is principally involved in the distribution of mobile phones and allied products of the two leading brands in the mobile industry; Huawei and Samsung. The company has also recently been awarded the distribution rights of Iphone in the country in collaboration with a Singaporean group. Additionally, the company has also signed an agreement with Tecno for distribution services. Airlink is associated with Huawei and Samsung since 2012 and 2016 respectively.

Ownership

Ownership Structure The company is owned by the sponsoring family; formerly by two brothers - Mr. Muazzam Hayat Piracha (Late) and Muzaffar Hayat Piracha. After the death of Mr. Muazzam Hayat Piracha, his shares have been transferred to his wife, Ms. Saliha Basit (~5%) and his four daughters (~6% each). Mr. Shaukat Hayat Piracha, paternal uncle of the two pioneer owners, has lately transferred his stake to his son, Mr. Yasir Hayat Piracha who now owns 30% shares in the company.

Stability No change in shareholding pattern has occurred in the period under review. Settlement of Mr. Muazzam's shareholding among his family members represents stability.

Business Acumen Mr. Muzaffar Hayat - the main sponsor, is leading the company since its inception. He is a seasoned professional possessing strong understanding of the industry. Business acumen is, therefore, considered good.

Financial Strength Owners of the company do not have any strategic stake in other companies. Mr. Muzaffar owns residential properties. Financial strength is, therefore, considered adequate.

Governance

Board Structure Airlink is transforming its governance structure to cope with the compliance of Code of Corporate Governance, for which appointment of three independent directors has been done. Other than the independent directors, there are four members on the Board.

Members' Profile Board member's business acumen is considered good as they have vast experience of the relevant industry. Mr. Aslam Hayat Piracha, carrying extensive experience in the relevant field, is the Chairman of the Board.

Board Effectiveness The board has two sub-committees; Audit and HR & Remuneration Committee, which enables the board to keep an oversight of the business more closely.

Financial Transparency An Internal Audit department reporting independently to the Audit Committee is in place. EY Ford Rhodes Chartered Accountants are the External Auditors, category 'A' rated firm of SBP. They have expressed an unqualified opinion on the company's financial statements for FY19.

Management

Organizational Structure Airlink has a well-defined organizational structure and different types of activities are properly segregated and managed through different departments. The department heads report to the CEO & respective heads.

Management Team Mr. Muzaffar Hayat Piracha, CEO of the company, is an MBA and has been associated with the company since its inception. Mr. Muzaffar resides in Lahore Head Office and is involved in all strategic and key decisions of the company.

Effectiveness There are six management committees operating namely as; i) Credit Committee, ii) Risk Management Committee, iii) Sale Control Committee, iv) Cash Management Committee, v) Operational Control Committee and vi) Business Plan Committee, which help in ensuring operational efficacy.

MIS Airlink has installed SAP-an ERP solution as its information system, which provides adherence to a sound reporting system within the company.

Control Environment MIS reports for senior management are generated frequently and are detailed in nature. Many reports, including the following, are generated frequently of each business unit: 1) Region wise business partner report including adjustments, 2) daily stock report for all warehouses 3) product wise report of region and corporate limits.

Business Risk

Industry Dynamics Historically, Pakistan has been one of the fastest growing cellular markets on the globe. The country's teledensity increased from 6% in FY04 to a high of 77% in 1QFY20. Smartphone penetration in total mobile phone market is growing but is still low which creates an opportunity for the smart phone manufacturers as well as its distributors. The recent imposition of Device Identification Registration and Blocking System (DIRBS) has reduced the proportion of grey channel import market in the system, which is another added benefit to the legal authorized importers. However, at the same time, rapid devaluation of currency against USD has amplified the prices of imported phones, thus gradually impacting the demand, especially of high-end range mobile phones. The industry is entirely dependent on imports. The rise in duty structure has had a negative impact on the overall imports in the country, with volumes falling in FY19, compared to the prior year. In FY19, Samsung was the most imported brand (41%), followed by Huawei (14%) and Oppo (8%).

Relative Position Airlink is one of the 4 mobile phone distributors of the country. The company is working with the world's top brands of mobile phones. Huawei and Samsung both contribute ~50% to the company's revenue. Recent award of distribution rights of Apple and Tecno phones is boding well for sustaining system share of the company.

Revenues During FY19, the company recorded a topline of PKR~29,786m (FY18: ~24,151m), depicting a wholesome growth of 23% YoY. Meanwhile, it earned a revenue of PKR~7,939m during 3MFY20, representing an annualized growth of 7% compared to FY19. Huawei is the major contributor in the company's total revenue. Rising prices have played a major role in expanding the topline. As Huawei quantum share declined in 1QFY20, diversity, including iphone and tecno distribution, is initiated to keep the business volumes intact.

Margins Margins have remained intact. In 3MFY20, gross profit margin clocked in at 15.3% (FY19: 13.4%, FY18: 13.0%). Favorable pricing has played a major role in raising the margins. A similar trend was noted in the net profit margins (3MFY20: 5.7%, FY19: 5.0%, FY18: 5.1%).

Sustainability The company is intending to improve its overall organisation structure alongside growth in business. Going Listed on the PSX is on cards and the process has been initiated. Proactive management strategies to aptly manage hindrances in growth are essential. Airlink has been successful in subduing the expected volumetric decline of Huawei by replacing the foregone Huawei offtake with the sales of a new brand - Tecno. Additionally, the company has also been awarded the distribution rights of Apple phones in the country, in collaboration with a Singaporean Group.

Financial Risk

Working Capital Working capital requirement emanates from financing trade receivables and inventory. Since the imposition of SBP's directive to maintain 100% margin for Line of Credit (LC), working capital needs have elevated. Short term borrowings (STBs) have also gone high on the scale. Thereby, the company's short term trade leverage has gone negative depicting no further cushion of trade assets available against STBs. The average gross working capital days, albeit high, have stayed consistent in the recent past (3MFY20: 72 days, FY19: 75 days, FY18: 75 days). A similar trend was noted in the average net working capital days of the company (3MFY20: 41 days, FY19: 42 days, FY18: 43 days).

Coverages Core operating coverages have been part of a falling trend mainly due to an increased interest cost (3MFY20: 2.3x, FY19: 3.0x, FY18: 4.7x). Debt payment capacity, currently remains comfortable.

Capitalization Total debt of the company considerably increased in FY19. At End-3MFY20, it clocked in at PKR~7,569m (End-FY19: PKR~7,873m, End-FY18: PKR~4,286m). The company has a highly leveraged capital structure. At End-3MFY20 leveraging stood at 68.5% (End-FY19: 72.1%, End-FY18: 61.7%). Most of the debt book is composed of short term loans to manage working capital needs. Cautious management approach is necessitated.



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Financial Summary

PKR mln

Airlink Communication Pvt Limited Communication	Sep-19 3M	Jun-19 12M	Jun-18 12M	Jun-17 12M
A BALANCE SHEET				
1 Non-Current Assets	356	323	130	99
2 Investments	1,503	2,490	1,226	-
3 Related Party Exposure	-	-	-	-
4 Current Assets	13,354	12,155	8,830	5,690
a Inventories	1,755	1,118	2,171	1,789
b Trade Receivables	4,575	5,125	3,882	2,069
5 Total Assets	15,213	14,968	10,187	5,789
6 Current Liabilities	4,013	3,930	3,227	1,594
a Trade Payables	2,744	2,611	2,838	1,427
7 Borrowings	7,569	7,873	4,286	2,068
8 Related Party Exposure	81	72	-	-
9 Non-Current Liabilities	27	23	17	2
10 Net Assets	3,524	3,069	2,656	2,124
11 Shareholders' Equity	3,524	3,069	2,656	2,124
B INCOME STATEMENT				
1 Sales	7,939	29,786	24,151	13,275
a Cost of Good Sold	(6,727)	(25,799)	(21,004)	(11,438)
2 Gross Profit	1,213	3,986	3,147	1,837
a Operating Expenses	(171)	(740)	(515)	(383)
3 Operating Profit	1,041	3,246	2,632	1,454
a Non Operating Income or (Expense)	57	176	46	-
4 Profit or (Loss) before Interest and Tax	1,098	3,422	2,678	1,454
a Total Finance Cost	(337)	(827)	(388)	(146)
b Taxation	(306)	(1,115)	(1,056)	(633)
6 Net Income Or (Loss)	455	1,480	1,234	674
C CASH FLOW STATEMENT				
a Free Cash Flows from Operations (FCFO)	690	2,248	1,647	704
b Net Cash from Operating Activities before Working Capital Changes	440	1,833	1,349	704
c Changes in Working Capital	(910)	(4,660)	(1,524)	(2,110)
1 Net Cash provided by Operating Activities	(470)	(2,827)	(175)	(1,406)
2 Net Cash (Used in) or Available From Investing Activities	991	(11)	(1,282)	(66)
3 Net Cash (Used in) or Available From Financing Activities	(434)	2,730	1,513	1,257
4 Net Cash generated or (Used) during the period	87	(109)	56	(215)
D RATIO ANALYSIS				
1 Performance				
a Sales Growth (for the period)	6.6%	23.3%	81.9%	32.6%
b Gross Profit Margin	15.3%	13.4%	13.0%	13.8%
c Net Profit Margin	5.7%	5.0%	5.1%	5.1%
d Cash Conversion Efficiency (EBITDA/Sales)	11.5%	11.3%	10.9%	10.2%
e Return on Equity (ROE)	55.2%	51.7%	51.6%	41.4%
2 Working Capital Management				
a Gross Working Capital (Average Days)	72	75	75	133
b Net Working Capital (Average Days)	41	42	43	96
c Current Ratio (Total Current Assets/Total Current Liabilities)	3.3	3.1	2.7	3.6
3 Coverages				
a EBITDA / Finance Cost	3.0	4.5	7.5	10.8
b FCFO / Finance Cost+CMLTB+Excess STB	2.2	3.0	4.5	5.2
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)	0.6	0.6	0.0	0.0
4 Capital Structure (Total Debt/Total Debt+Equity)				
a Total Borrowings / Total Borrowings+Equity	68.5%	72.1%	61.7%	49.3%
b Interest or Markup Payable (Days)	76.4	117.8	51.3	123.4
c Average Borrowing Rate	15.5%	12.1%	11.1%	7.9%

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		Short Term Ratings	
AAA	Highest credit quality. Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments	A1+	The highest capacity for timely repayment.
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.	A1	A strong capacity for timely repayment.
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.	A2	A satisfactory capacity for timely repayment. This may be susceptible to adverse changes in business, economic, or financial 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.	A3	An adequate capacity for timely repayment. Such capacity is susceptible to adverse changes in business, economic, or financial conditions.
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	The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions.
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.	C	An inadequate capacity to ensure timely repayment.
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.		



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 surveil the opinion due to lack of requisite information.

Harmonization A change in rating due to revision in applicable methodology or underlying scale.

Disclaimer: PACRA's ratings are an assessment of the credit standing of entities/issue in Pakistan. They do not take into account the potential transfer / convertibility risk that may exist for foreign currency creditors. PACRA's opinion is not a recommendation to purchase, sell or hold a security, in as much as it does not comment on the security's market price or suitability for a particular investor.

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

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- (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.
- (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)
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- (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)
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- (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)

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- (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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