



The Pakistan Credit Rating Agency Limited

Rating Report

Brainchild Communications Pakistan (Pvt.) Limited

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Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
12-Sep-2019	BBB	A3	Stable	Initial	-

Rating Rationale and Key Rating Drivers

The ratings reflect Brainchild's ability to uphold its relative market position in its respective niche of the advertising arena. With a portfolio of sound multinational clientele, the Bee Squared Group (Brainchild, Blitz and Z2C Pakistan), grasps a prominent position in the related market. Strength is derived from the diverse yet competing customer base of the companies. Sponsor acumen provides comfort to the ratings as is evidenced through well-devised corporate strategies. Additionally, association of an International media brand and support of a team of energetic individuals bodes well for the business prospects. The operating segment of the company is directly influenced by the pattern of advertising expenditure in the economy. Profitability has fallen in the recent past, owing to lower number of fresh mega launches. Inclination towards digital domain is, however pacing up. The concept of Brainchild functioning as a bridge between clients and media entails timely delivery of services and payments; key recipe is prudent cash management. Brainchild has chalked out strategies to avail benefits of its liquidity management schemes. This income stream nurtures the company's bottomline margin, in the absence of which the profitability falls thin. Financial risk profile is displayed by adequate coverages and leveraged capital structure. Borrowings majorly constitute short term lines availed from a foreign commercial bank to fund working capital needs and optimize cash management operations.

The ratings are dependent on the management's ability to sustain the market position amidst fierce competition and changing business environment. Profit generation from core business remains critical. Meanwhile, financial metrics including but not limited to working capital management and debt coverage must be upheld.

Disclosure

Name of Rated Entity	Brainchild Communications Pakistan (Pvt.) Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	PACRA_Methodology_Corporate_FY19(Jun-19),PACRA_Criteria_LT ST Relationship_FY19(Jun-19)
Related Research	Sector Study Media(Jun-19)
Rating Analysts	Muhammad Usman muhammad.usman@pacra.com +92-42-35869504

Profile

Legal Structure Brainchild Communications Pakistan (Pvt.) Limited (herein referred to as "Brainchild" or "the company") is a Private Limited Company incorporated, as a majority owned subsidiary of Bee Squared (Pte.) Limited, in 2010.

Background The company was incorporated under the Companies Ordinance, 1984 (now "Companies Act, 2017"), as a full-service agency operating in the space of communication & media. In the year of its inception, i.e., 2010, the company entered into a franchising agreement (non-ownership) with Publicis Groupe, one of the largest media houses in the world. It is based in France. The company uses the trademark of the divisions of the Publicis Group; Starcom and Mediavest.

Operations Brainchild's principal activity is to carry out media buying and planning for its clients. Moreover, it specializes in media consulting and other related activities including media research and creative services, with respect to digital marketing. The company has three offices in the country i.e. in Karachi, Lahore and Islamabad.

Ownership

Ownership Structure Brainchild is majority owned by Bee Squared PTE (52%), a company based in Singapore. The rest of the shareholding belongs to Mr Raihan Merchant, the chairman of Brainchild (38%) and Merchant Holdings (Pvt.) Ltd (10%), a fully owned company of Mr. Raihan Merchant.

Stability The ownership of the company has not changed since its inception. There is a formal succession plan in place.

Business Acumen Mr. Raihan Merchant, the founding chairman of Brainchild, is considered a pioneer in the field of media and advertising. He introduced the concept of media buying in the country. In 2011, the Government of Pakistan awarded him the Tamgha-e-Imtiaz (Medal of Excellence), recognizing his contributions to the advertising industry of Pakistan. Making use of its affiliation with a world recognized marketing group, the company has demonstrated sanguine performance indicators and growth on a consistent basis, depicting strong business acumen.

Financial Strength Financial strength of the sponsors is considered adequate.

Governance

Board Structure Board of Directors consists of four members, including the chairman and CEO of the company, along with two independent directors. The company is expected to increase the size of its board by the end of CY19, by increasing the representation of independent directors.

Members' Profile The board members have a strong professional background, with experience of over 30 years of all the directors, which brings vast expertise and knowledge to the table.

Board Effectiveness The board, having a blend of seasoned entrepreneurs and financial experts, supports the management in terms of strategic guidance. In line with the guidelines of Code of Corporate Governance, the Board has formed two sub-committees – (i) HR Committee and (ii) Audit Committee

Financial Transparency The auditors of the company, KPMG Taseer Hadi & Co, expressed an unqualified opinion on the financial statements for FY18

Management

Organizational Structure The organizational structure of the company is divided into thirteen functional departments headed by able professionals, who report directly to the Chairman and the CEO depending upon their department. The management consists of professionals having long association with Brainchild. The company rotates its employees within different departments, enabling them to gather varied expertise; hence providing a succession line for the senior management.

Management Team Mr. Syed Taqui Abbas Rizvi, the CEO of the company, has over 40 years of diversified professional experience in different sectors including finance, media, journalism, manufacturing, education, automobile and textile. He is a senior Fellow member of the Institute of Chartered Accountants of Pakistan. He is supported by a competent management team, consisting of experienced professionals.

Effectiveness Currently, the company does not have any formal management committees. All pertinent issues are resolved at department levels by the department managers and heads.

MIS The company has both in-house as well as globally-sourced tools (both licensed and proprietary) which allow it to provide high level of insight, optimization and value to its clients. Brainchild uses Oracle and Telesolutions as its ERP software.

Control Environment The departments are layered into various cadres of management to define clear lines of responsibilities and authorization, accompanied by a technological infrastructure for all its manufacturing and support functions. Management meetings take place frequently, to discuss the company's financial position and future strategy.

Business Risk

Industry Dynamics The consumer preferences and trends change rapidly in the industry. To keep intact the market share, the players must have an agile and data-centered approach to planning. The total advertising expenditure in the country for FY19, amounted to PKR ~84.7bln (FY18: ~86.4bln).

Relative Position The company holds a prominent position in the market. The industry consists of two major players; Group M and Brainchild. With respect to the advertising expenditure on TV, during FY19, Group M is the market leader with ~44% market share, while Brainchild is second with ~18% market share. The rest of the market belongs to smaller players in a largely fragmented market.

Revenues The revenue of the company, consists of both service income and discounts, as a result of effective cash management. The total topline for 9MFY19 amounted to PKR ~535mln, compared to PKR ~478mln in 9MFY18, showcasing a healthy increase of 12%. Due to the macro-economic outlook, in FY19, there has been an overall decrease in the advertising expenditure in the industry. In spite of such challenges, BCP has been able to maintain its revenue.

Margins The company's overall profit margins continue to improve. Gross profit margin for 9MFY19 clocked in at 22.7% (9MFY18: 15.5%), while the net profit margin stood at 8.4% (9MFY18: 5.0%). It is to be reiterated, that the profit margins have improved mainly as a result of the rise in income from discounts, during 9MFY19.

Sustainability Application for licenses of 40 new TV channels have been submitted to PEMRA. Regardless of the economic conditions, the clients are expected to continue spending on advertising as it is a necessity for the entities to reach the end consumer. Prospective clients in the Telecommunication and Microfinance Banking sectors, are expected to join the portfolio of the company.

Financial Risk

Working Capital Due to the nature of the business, the total billings (which are to be subsequently paid to the media suppliers) form part of the trade receivables and payables. The working capital cycle is calculated with reference to the total billings as opposed to the revenue of the company. As at 9MFY19, the trade receivable days have decreased to 103 days (FY18: 113 days). On the other hand, the trade payable days have dropped to 83 days (FY18: 99 days). Consequently, net working capital cycle has been negatively impacted, increasing to 20 days, compared to 13 days in FY18.

Coverages The free cash flows (FCFO) of the Company during 9MFY19 stood at PKR ~132mln (9MFY18: PKR ~56mln), representing a massive increase of 137% YoY. The increase is largely attributable to a rise in revenue of the company leading to a higher EBITDA. FCFO coverage to debt obligations (finance cost, CMLTD and uncovered short term borrowing) stands at 0.8 times, improving from 0.3 times (9MFY18).

Capitalization During 9MFY19, leveraging of the company has risen. Leveraging mix majorly comprises of short-term foreign currency loans, amounting to PKR~776mln (FY18: PKR~652mln), which are secured against the receivables of the company. As a result, the leveraging clocked in at 67% (FY18: 66%), which is considered high. The devaluation of the PKR has also played a role in this regard. The company, after paying off its entire current debt, is expected to continue its financing behavior, required for; further income generation from sources, such as volume and payment discounts, along with development projects relating to the group companies.



The Pakistan Credit Rating Agency Limited

Financial Summary

PKR mln

	Mar-19	Jun-18	Jun-17	Jun-16
	9M	12M	12M	12M

A BALANCE SHEET

1 Non-Current Assets	253	236	154	163
2 Investments	17	17	19	-
3 Related Party Exposure	280	356	326	395
4 Current Assets	2,377	2,141	2,473	2,307
<i>a Inventories</i>	-	-	-	-
<i>b Trade Receivables</i>	2,216	2,069	2,423	2,272
5 Total Assets	2,927	2,750	2,972	2,864
6 Current Liabilities	1,745	1,733	2,255	2,399
<i>a Trade Payables</i>	1,731	1,724	2,233	2,364
7 Borrowings	787	667	413	223
8 Related Party Exposure	-	-	-	-
9 Non-Current Liabilities	0	0	0	0
10 Net Assets	394	349	304	242
11 Shareholders' Equity	394	349	304	242

B INCOME STATEMENT

1 Sales	535	722	670	758
<i>a Cost of Good Sold</i>	(414)	(605)	(558)	(621)
2 Gross Profit	122	116	112	138
<i>a Operating Expenses</i>	-	-	-	-
3 Operating Profit	122	116	112	138
<i>a Non Operating Income or (Expense)</i>	11	24	7	20
4 Profit or (Loss) before Interest and Tax	133	141	119	158
<i>a Total Finance Cost</i>	(56)	(48)	(32)	(19)
<i>b Taxation</i>	(32)	(47)	(26)	(54)
6 Net Income Or (Loss)	45	46	62	84

C CASH FLOW STATEMENT

<i>a Free Cash Flows from Operations (FCFO)</i>	132	111	93	130
<i>b Net Cash from Operating Activities before Working Capital Changes</i>	84	65	65	111
<i>c Changes in Working Capital</i>	(81)	(178)	(231)	(222)
1 Net Cash provided by Operating Activities	4	(113)	(166)	(111)
2 Net Cash (Used in) or Available From Investing Activities	(57)	(106)	(26)	(142)
3 Net Cash (Used in) or Available From Financing Activities	120	254	189	172
4 Net Cash generated or (Used) during the period	68	36	(3)	(81)

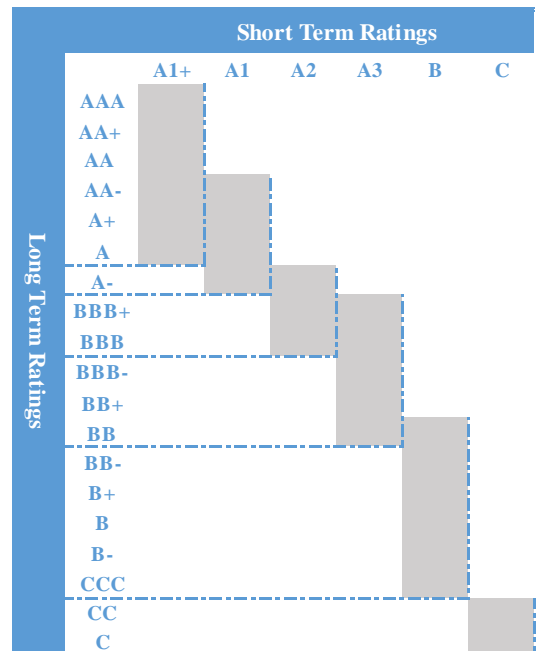
D RATIO ANALYSIS

1 Performance				
<i>a Sales Growth (for the period)</i>	-1.1%	7.7%	-11.6%	26.1%
<i>b Gross Profit Margin</i>	22.7%	16.1%	16.7%	18.2%
<i>c Net Profit Margin</i>	8.4%	6.3%	9.2%	11.1%
<i>d Cash Conversion Efficiency (EBITDA/Sales)</i>	31.8%	24.5%	20.1%	22.8%
<i>e Return on Equity (ROE)</i>	16.1%	14.0%	22.6%	34.8%
2 Working Capital Management				
<i>a Gross Working Capital (Average Days)</i>	103	113	126	107
<i>b Net Working Capital (Average Days)</i>	20	13	3	-4
<i>c Current Ratio (Total Current Assets/Total Current Liabilities)</i>	1.4	1.2	1.1	1.0
3 Coverages				
<i>a EBITDA / Finance Cost</i>	3.2	3.8	4.6	9.2
<i>b FCFO / Finance Cost+CMLTB+Excess STB</i>	0.8	0.4	0.4	0.4
<i>c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)</i>	1.5	4.0	3.1	2.8
4 Capital Structure (Total Debt/Total Debt+Equity)				
<i>a Total Borrowings / Total Borrowings+Equity</i>	66.6%	65.6%	57.6%	48.0%
<i>b Interest or Markup Payable (Days)</i>	69.7	55.8	61.5	29.7
<i>c Average Borrowing Rate</i>	9.8%	8.6%	9.3%	8.4%

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

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.

(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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