The Pakistan Credit Rating Agency Limited

Rating Report

Pakistan Mobile Communications Limited

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
26-May-2021	AA	A1	Stable	Upgrade	-
29-Jun-2020	AA-	A1	Positive	Maintain	-
08-Nov-2019	AA-	A1	Positive	Maintain	-
10-May-2019	AA-	A1	Positive	Maintain	-

Rating Rationale and Key Rating Drivers

The ratings incorporate the robust business profile of the company, represented by its leading market share of ~38% with ~69 million cellular subscribers as at March 21. Cellular market is dominated by three large players and they collectively possess 85% of market share, whereas 65% of market is preliminary in the hands of two players Jazz & Telenor. Teledensity has now reached up to 85% and significant barriers for new entrants are now in place; the market may experience consolidation in future. The outbreak of COVID-19 pandemic has intensified the usage of high speed 3G/4G data technology, currently there are 98 million 3G/4G subscribers and Jazz holds the position of market leader and was able to achieve remarkable growth in 4G subscribers (61%) during CY20. Overall market dimension remained positive in CY20 with respect to penetration level in 3G/4G subscribers which is now reached up to ~44%. Rating takes comfort from formidable sponsors support and strong business volumes/margins. Additionally, the company is pursuing digitalization as a long-term strategy and vision. The Company's financial risk profile exhibits a stable outlook demonstrated by eased working capital strategies, comfortable coverages and moderate leveraging (Dec'20). Notable CAPEX is incurred by the company on a periodic and need basis, owing to the nature of the business. Debt profile majorly comprises long term borrowings. Jazz made partial payment for renewal of 2G license USD~270mln as under protest fee (total payment demand by PTA is USD~450mln) necessitated additional external capital dependence. Total on-balance sheet debt level, however, continued to align with the previous trend, as some portion of the previous debt book retired in CY20.

The ratings are dependent upon the sustenance of leading market position, robust revenue growth and profitability, and vigorous financial matrix. As capital structure becomes leveraged, maintenance of sound financial discipline is imperative to hold.

Disclosure

Name of Rated Entity	Pakistan Mobile Communications Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology | Corporate Ratings(Jun-20),Methodology | Correlation Between Long-Term And Short-Term Rating Scale(Jun-20),Criteria | Rating Modifier(Jun-20)
Related Research	Sector Study | Communication(May-20)
Rating Analysts	Kanwal Ejaz | kanwal.ejaz@pacra.com | +92-42-35869504

Profile

Legal Structure Incorporated in 1990, Pakistan Mobile Communications Limited ("the company") is a public unlisted company. The head office of the company is in Islamabad.

Background PMCL was incorporated in Pakistan in December 1990 as private limited company, and commenced operations in August 1994. In February 2005, the company changed its status from a private limited company to a Public Limited company. PMCL was initially also rated by international rating agencies due to its foreign debt exposure.

Operations Pakistan Mobile Communications Limited (PMCL) is the largest cellular telecommunication service provider of the country engaged in installation, operation and maintenance of a countrywide GSM cellular network under the brand name of Jazz.

Ownership

Ownership Structure VEON owns 100% shareholding of the company, 85% through wholly owned subsidiary International Wireless Communications Pakistan Ltd and 15% stake through another wholly owned subsidiary VEON Pakistan Holdings B.V.

Stability Ownership structure is expected to remain stable with clear representation on the governance side.

Business Acumen VEON offers a wide range of wireless, fixed and broadband services to approximately 214mln customers in 9 countries. The group (formerly Vimplecom) has rebranded to VEON through revitalizing its business operations from telecom to wider technology platforms in order to penetrate in diversified streams.

Financial Strength During CY20, VEON Ltd revenue clocked in at USD 7,980mln (CY19: USD 8,864mln) and EBITDA stood at USD 3,453mln.

Governance

Board Structure PMCL’s Board of Directors comprises seven members including Chief Executive Officer.

Members’ Profile The board comprises highly qualified and experienced professionals holding senior positions in the group companies.

Board Effectiveness PMCL’s Board of Directors comprises seven members including Chief Executive Officer. All are seasoned professional with vast experiences.

Financial Transparency The Auditors of the company, A.F.Ferguson & Co. expressed an unqualified opinion on the company’s financial statements for the year ended December 31, 2020. The internal audit function of the company is in-house and reports directly to the board.

Management

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

Management Team Mr. Aamir Ibrahim has over two decades experience in blue chip companies across various countries and industries, but majorly of telecom sector.

Effectiveness The top management possess quality education from distinguished educational institutions both local and international. As well as both local and foreign experience. In PMCL’s reporting structure, chief holds the senior most position followed by the VP ,Director/Senior Manager and then the manager and Associates.

MIS The company is using Oracle based ERP system (different modules) which is fully integrated amongst all back-end departments of the company.

Control Environment Report generation has been optimized to bring efficiency. The management of PMCL reports at the Group level on a monthly basis via presentation on performance and key KPIs.

Business Risk

Industry Dynamics The country's total number of cellular subscribers reached to 183 million users by March-21 (penetration of ~84% of the total market) while 3G/4G subscribers reached to 98 million users (penetration of 44%). The rate of growth in 3G/4G subscribers has been impressive in the last few years.

Relative Position The company relishes on a share of ~38% in market cellular subscribers followed by Telenor which has a 27% market share, Zong with 22.06% market share, while Ufone has 13% of market share respectively. Jazz also leads the market in term of 3G/4G subscribers Jazz 4G subscribers stood at 29mln by the end of March 2021.

Revenues During CY20, PMCL’s revenue clocked at PKR 199,280mln (CY19: 197,481mln). In terms of ARPUs, average voice ARPU recorded at PKR 86 per user in CY20 with ~26% decrease on YoY basis (Dec19: PKR 115), average data ARPUs recorded at PKR~139 per user with 9% growth on YoY basis (Dec'19: PKR 127). The outbreak of COVID-19 pandemic has intensified the usage of 3G/4G technology.

Margins Improved sales translated into improved profit margins, Net profit margin of the company reached to ~18% during CY20 (CY19: 17.2%).

Sustainability Jazz successfully tested out the fifth generation of mobile technology at the Jazz Digital Headquarters in Islamabad in January 2020. Going forward, the company, would continue its efforts to further strengthen its market position as the leading cellular provider. Focus would remain towards data monetization to improve profitability margins. Furthermore, PMCL, using the platform of Mobilink Microfinance Bank, an associate entity, intends to establish a strong digital platform.

Financial Risk

Working Capital The business of the Company is cash-centric, as is witnessed from an EBITDA to Sales ratio of 49.8% in CY20 (CY19: 50.7%). Healthier EBITDA would enable the Company in meeting the remaining 2G license renewal fees (paid payment of USD 270mln) with ease. This fee has been made under protest and the remaining is contingent upon high court’s order.

Coverages Company has incurred PKR~42bln of capex which stands at 21% of revenue. The Company’s Debt and Interest coverage remained strong On backdrop of strong FCFO.

Capitalization The company’s debt burden is skewed towards long term borrowings. Company's Total Borrowings/Borrowings plus Equity is ~31.8% as on December 2020 (Dec’19:~34.3%).

The Pakistan Credit Rating Agency Limited

Financial Summary
PKR mln

PAKISTAN MOBILE COMMUNICATIONS LIMITED COMMUNICATIONS	Dec-20 12M	Dec-19 12M	Dec-18 12M	Dec-17 12M
A. CAPITAL STRUCTURE				
1 Share Capital	48,019	48,019	48,019	48,019
2 Shareholder's Equity	145,488	136,426	125,779	97,330
a. Total Borrowings/(Total Borrowings + Equity)	31.8%	34.3%	33.5%	49%
B. BUSINESS ANALYSIS				
1 Sale	199,280	197,481	181,722	160,679
a. Sale Growth	0.9%	8.7%	13.1%	5.9%
b. Revenue to Equity	4.2	4.1	3.8	3.3
2 Profit or (loss) before interest and tax	64,357	64,212	49,731	36,122
3 Net Income or (Loss)	35,931	33,984	16,774	12,783
a. Net profit Margin	18%	17.2%	9.2%	8%
b. Return on Equity	25%	25%	13%	13%
c. Current ratio	0.17	0.1	0.2	0.1
C. CASH FLOW POSITION				
1 Earnings before Interest, Tax, Depreciation and Amortization (EBITDA)	99,188	100,074	86,811	74,096
a. Cash Conversion Efficiency(EBITDA/Sales)	49.8%	50.7%	47.8%	46.1%
2 Free Cash Flow from Operations (FCFO)	57,312	67,296	62,887	48,831
a. Cash Conversion Efficiency (FCFO/Sales)	28.8%	34.1%	34.6%	30.4%

Credit Rating

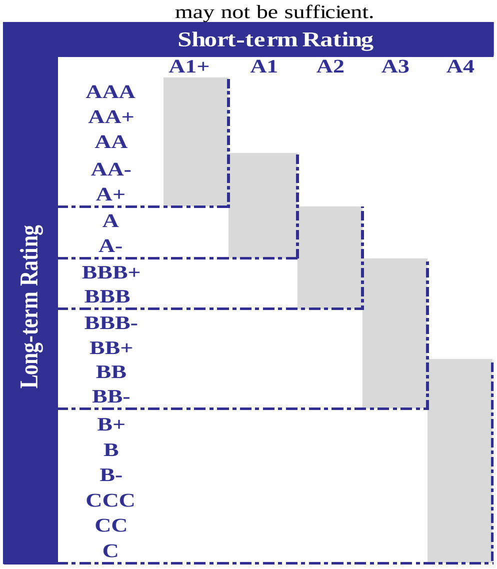
Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

Long-term Rating

Scale	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 Rating

Scale	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
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 surveill 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):

Entities
a) Broker Entity Rating
b) Corporate Rating
c) Financial Institution Rating
d) Holding Company Rating
e) Independent Power Producer Rating
f) Microfinance Institution Rating
g) Non-Banking Finance Companies (NBFCs) Rating

Instruments
a) Basel III Compliant Debt Instrument Rating
b) Debt Instrument Rating
c) Sukuk Rating

Regulatory and Supplementary Disclosure

(Credit Rating Companies Regulations,2016)

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)

Proprietary Information