The Pakistan Credit Rating Agency Limited

Rating Report

Pakistan Mobile Communications Limited | Sukuk | Dec-14

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
10-May-2019	AA	-	Positive	Maintain	-
08-Nov-2018	AA	-	Positive	Maintain	-
27-Apr-2018	AA	-	Positive	Maintain	-
14-Nov-2017	AA	-	Positive	Maintain	-
22-Mar-2017	AA	-	Positive	Maintain	-
22-Mar-2016	AA	-	Rating Watch	Maintain	-
30-Apr-2015	AA	-	Stable	Maintain	-
19-Dec-2014	AA	-	Stable	Initial	-
19-May-2014	AA	-	Stable	Preliminary	-
07-Jan-2014	AA	-	Stable	Preliminary	-

Rating Rationale and Key Rating Drivers

The ratings incorporate robust business profile of the company, represented by a leading market share of ~37% with ~58 million cellular subscribers as at End-March’19. This strong share has been achieved with organic and inorganic growth. The company enjoys synergies related to operational and technical network, reflected into better earnings for the merged entity. Optimizing on its single brand "Jazz", the company commands solid volumes and strong margins. Additionally, in collaboration with Mobilink Microfinance Bank, an associate entity, the company is establishing a strong digital banking platform. Overall market dimensions remain positive, particularly in mobile data services, as penetration level in 3G/4G subscribers stands at ~32% as at End-March’19, depicting sufficient room for growth. Tax is again being deducted on mobile top ups and services, which will normalize the growth in future periods. The company's financial risk profile exhibits a strong outlook demonstrated by prudent working capital strategies and comfortable coverages. Company’s 2G license, acquired through acquisition of Warid, is due to expire on 26th May 2019. Uncertainty, regarding renewal of license is continue to prevail as the PTA has not yet issued the Information Memorandum (IM) stating the term of license. However, the company has obtained the stay order from Islamabad High Court to continue operation until the renewal of license. The company has invested PKR 28,123bln in money market funds and treasury bills, which reflects available liquidity cushion.

The ratings are dependent upon the sustenance of robust revenue growth and profitability. Positive outlook captures the leading market position of the company and the strong financial indicators along with improvement in capital structure. The company’s ability to maintain its market position along with smooth continuation of operations is pertinent to the ratings. Meanwhile, growth in average revenue per user of the company is also considered important.

Disclosure

Name of Rated Entity	Pakistan Mobile Communications Limited	Sukuk	Dec-14
Type of Relationship	Solicited
Purpose of the Rating	Debt Instrument Rating
Applicable Criteria	Methodology	Corporate Ratings(Jun-18),Methodology	Sukuk(Jun-18),Methodology	Debt Instrument(Jun-18)
Related Research	Sector Study	Mobile Telecom(May-19)
Rating Analysts	Muhammad Nadeem Sheikh	nadeem.sheikh@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 The company was formerly known as Mobilink. However, after the merger with Warid Telecom Pakistan mid 2016, both companies re-launched under the brand name "Jazz".

Operations The company is the largest cellular telecommunication service provider of the country, engaged in installation, operation and maintenance of a countrywide cellular network under the brand name "Jazz". It holds four separate 2G licenses, one 3G and one 4G license.

Ownership

Ownership Structure Ownership of the company lies with Veon (formerly Vimplecom). However, after issuance of ~15% stake to Warid's sponsor - Dhabi Group, following merger, its stake diluted to ~85%.

Stability Ownership structure is expected to remain stable with clear representation on the governance bodes well for the company.

Business Acumen The company's ultimate sponsor - Veon is a multinational telecommunication services company, headquartered in Amsterdam, Netherlands. It is the sixth largest mobile network operator in the world by the number of subscribers. Most of the company's revenue streams from Russia. Sponsor acumen is, therefore, considered strong.

Financial Strength Veon - the ultimate parent, has investments and shareholding in a number of companies forming part of the group, spread across a widespread geographical scale.

Governance

Board Structure The Board of Governance is composed of ten members, including the CEO. Most of the members are representative of Veon.

Members' Profile The Board members are equipped with profound knowledge and expertise of the related business. His Highness Sheikh Nahayan Mabarak Al Nahayan, senior member of Royal Family and Minister of Culture, Youth and Community Development, UAE, is the Chairman of the Board. The board includes two executive directors, including the CEO and CFO.

Board Effectiveness Attendance recorded during the board meetings was satisfactory for the period under review. Minutes of the board meeting was detailed.

Financial Transparency M/S. A.F. Ferguson & Co. Chartered Accountants, one of the big four network firms, are the External Auditors of the company.

Management

Organizational Structure The company has a well-defined organizational structure with clear lines of responsibility and cadre dedicated within each department.

Management Team An experienced top management team with requisite background and qualification manages the operations. They are equipped with both local and foreign experience. Mr. Aamir Ibrahim – CEO of the company since July-16. He has over two decades experience of blue-chip companies across various countries and industries but majorly of telecom sector. He has recently been appointed as the Head of Emerging Markets at Veon group level.

Effectiveness All operations are monitored at the Department head level. KPIs and performance appraisal system to boost operational efficiencies are in place. The company has formally designated Management Committees for oversight of efficiency management.

MIS The company is using an analytical business intelligence reporting software to increase efficiency for employees and generate cost savings. The company has rolled out Oracle based ERP system which is fully integrated amongst all back-end departments of the company.

Control Environment Strong systems and controls under the supervision of the parent company are established and the same are continuously improving.

Business Risk

Industry Dynamics Pakistan Mobile Telecom Sector is composed of four players; Jazz, Telenor, Zong and Ufone. The industry has experienced various changing trends in the past few years due to smartphone penetration and emergence of high speed data service needs. Total number of cellular subscribers has reached to 159 million users by Mar-19 (penetration of ~75.87% of the total market) and 3G/4G subscribers have reached to 66 million users (penetration of 31.55%).

Relative Position The company relishes on a share of ~37% in market cellular subscribers, demonstrating a strong foothold in the segment, specially taking a boom after merger with Warid. It also has the highest number of 3G subscribers in the country, whereas in 4G technology, Zong takes the lead.

Revenues The company's consolidated net revenue clocked in at PKR~171,067mln in CY18, indicating a growth of ~13% YoY basis (CY17: PKR 151,196mln). The growth in revenue is came on back of subscribers growth, price rationalization and termination of taxes by Supreme Court. However, going forward revenue of the company is expected to get impacted by revival of indirect taxes on mobile top up and usage.

Margins Improving gross margin trend can also be witnessed in CY18 as the company's gross profit margin was 42% in CY18 as compare to 40% in CY17. Continuous, cost rationalization has also resulted in improved operating profit margin, the company generated operating profit margin of 27% during CY18 (CY17: 25%) .

Sustainability After the cancellation of the company's bid to enter in Sale Purchase Agreement (SPA) with EdotCo (a joint venture of Malaysian telecom group Axiata and Dawood Hercules group) to adopt "asset light business model" and sell its passive tower infrastructure business. The company is considering other options to achieve its objective of ''asset light business model''.

Financial Risk

Working Capital Cash conversion cycle is kept reasonably effective. Working capital is a function of the company's receivable and creditor days, which recorded at ~11 and ~32 days respectively during CY18 (CY17: ~15 and ~25 days). Cash conversion ratio (FCFO/Sales) increased to ~43% in CY18 (CY17: ~41%).

Coverages During 1HCY18, interest coverage remained strong, i.e., 12.5x (CY17: 15.5x), however, core and total coverages remained just above the line, due to a high portion of current maturity of long term debt. Going forward, in 2019, the company is expected to incur a wholesome expense on renewal of 2G spectrum acquired through Warid Telecom.

Capitalization The company's debt burden is concentrated in long term borrowings amounting to PKR~73,326mln as on End-Dec'18 (End-Dec'17: PKR~94,900mln). The company also added short term borrowings pf PKR 3,861mln during CY18. Equity stood at PKR~90,137mln as at End-Dec'18 (End-Dec'17: PKR~58,856mln), thereby forming a relatively leveraged capital structure, i.e., ~46% (End-Dec'17: ~62%).

PKR mln

The Pakistan Credit Rating Agency Limited

Pakistan Mobile Communication Limited

BALANCE SHEET	Dec-18 Annual	Dec-17 Annual	Dec-16 Annual
Non-Current Assets	**218,579**	**231,931**	**213,398**
Investments	**28,123**	**1,353**	**1,002**
Equity Instruments	-	-	-
Debt Instruments	28,123	1,353	1,002
Current Assets	**20,240**	**20,308**	**31,769**
Inventory	205	208	234
Trade Receivables	4,895	5,726	6,399
Others	15,140	14,374	25,136
Total Assets	**268,315**	**254,494**	**246,176**
Borrowings	**77,186**	**94,900**	**73,293**
Short-Term	3,861	-	-
Long-Term (Incl. CMLTB)	73,326	94,900	73,293
Other Short-Term Liabilities	98,027	95,863	86,255
Other Long-Term Liabilities	2,965	4,876	6,364
Shareholder's Equity	**90,137**	**58,856**	**80,264**
Total Liabilities & Equity	**268,315**	**254,494**	**246,176**
INCOME STATEMENT			
Sales	**171,067**	**151,196**	**128,751**
Gross Profit	72,131	60,972	49,673
Other Operating Income	8,235	10,551	4,856
Total Finance Cost	(7,014)	(5,413)	(4,672)
Net Income	**19,596**	**16,734**	**10,210**
CASH FLOW STATEMENT			
Free Cash Flow from Operations (FCFO)	73,625	62,192	45,243
Total Cashflows (TCF)	73,625	62,192	46,051
Net Cash changes in Working Capital	8,136	(5,887)	10,305
Net Cash from Operating Activities	74,985	52,600	52,808
Net Cash from InvestingActivities	(26,972)	(57,995)	(23,705)
Net Cash from Financing Activities	(25,047)	(2,666)	(17,086)
Net Cash generated during the period	22,966	(8,062)	12,017
RATIO ANALYSIS			
Performance			
Sales Growth (for the period)	13%	17%	29%
Gross Profit Margin	42%	40%	39%
Net Profit Margin	11%	11%	8%
Return of Equity	26%	24%	17%
Working Capital Management			
Gross Working Capital (Inventory Days + Receivable Days)	11.8	15	15
Net Working Capital (Inventory Days + Receivable Days - Payable Days)	-20.4	-10	1
Coverages			
Debt Service Coverage (FCFO / Finance Cost+CMLTB+Excess STB)	0.8	0.6	0.6
Interest Coverage (FCFO / Finance Cost)	12.5	15.5	12.7
Debt Payback (Total Long Term Debt+Excess STB) / (FCFO-Finance Cost)	1.9	2.9	3.0
Capital Structure (Total Debt/Total Debt+Equity)			
Capital Structure (Total Borrowings / Total Borrowings+Equity)	46%	62%	48%

Regulatory and Supplementary Disclosure

Nature of Instrument	Size of Issue (PKR)	Tenor	Security	Quantum of Security	Nature of Assets	Trustee	Book Value of Assets (PKR mln)
Sukuk	6,900 mln	5 years	1. 1st pari passu floating charge on all present and future assets 2. 1st pari passu floating charge on future and present collections of the company 3. Partial Credit Guarantee by GuarantCo.	25% over and above total value	Moveable Fixed Assets	Faysal Bank	150,000
				25% over and above total value	Receivable of the Company from debtors		150,000
				PKR 966mln	3rd party guarantee		0

Pakistan Mobile Communications Limited | Sukuk | Dec'14	
Name of Issuer	Pakistan Mobile Communications Limited
Issue size	PKR 6,900mln
Issue Date	Dec'14
Tenor	5 years
Maturity	22-Dec-19
Profit Rate	3 MK + 0.35%
Principal Repayment	12 equal installments of PKR 575mln commencing from 22-March-17
Security	1. 1st pari passu floating charge on all present and future assets 2. 1st pari passu floating charge on future and present collections of the company 3. Partial Credit Guarantee by GuarantCo.

Pakistan Mobile Communications Limited | Sukuk | Redemption Schedule

Due Date Principle*	Opening Principal	Principal Repayment*	Due Date Markup/ Profit*	Markup/Profit Rate	3M Kibor	Markup/Profit Payment	Installment Payable	Principal Outstanding
	PKR in mln					PKR in mln		
22-Dec-14	3,000							3,000
22-Mar-15			22-Mar-15	3 Month Kibor +0.88%	8.18%	68	68	3,000
22-Jun-15			22-Jun-15	3 Month Kibor +0.88%	6.88%	58	58	3,000
22-Sep-15	3,900		22-Sep-15	3 Month Kibor +0.88%	6.56%	56	56	6,900
22-Dec-15			22-Dec-15	3 Month Kibor +0.88%	6.49%	127	127	6,900
22-Mar-16			22-Mar-16	3 Month Kibor +0.88%	6.35%	125	125	6,900
22-Jun-16			22-Jun-16	3 Month Kibor +0.88%	6.09%	120	120	6,900
22-Sep-16			22-Sep-16	3 Month Kibor +0.88%	6.04%	119	119	6,900
22-Dec-16			22-Dec-16	3 Month Kibor +0.88%	6.11%	121	121	6,900
22-Mar-17		575	22-Mar-17	3 Month Kibor +0.88%	6.08%	120	695	6,325
22-Jun-17		575	22-Jun-17	3 Month Kibor +0.88%	6.08%	110	685	5,750
22-Sep-17		575	22-Sep-17	3 Month Kibor +0.35%	6.08%	92	667	5,175
22-Dec-17		575	22-Dec-17	3 Month Kibor +0.35%	6.15%	84	659	4,600
22-Mar-18		575	22-Mar-18	3 Month Kibor +0.35%	6.44%	78	653	4,025
22-Jun-18		575	22-Jun-18	3 Month Kibor +0.35%	6.92%	73	648	3,450
22-Sep-18		575	22-Sep-18	3 Month Kibor +0.35%	8.06%	73	648	2,875
22-Dec-18		575	22-Dec-18	3 Month Kibor +0.35%	10.53%	78	653	2,300
22-Mar-19		575	22-Mar-19	3 Month Kibor +0.35%	10.79%	64	639	1,725
22-Jun-19		575	22-Jun-19	3 Month Kibor +0.35%	10.79%	48	623	1,150
22-Sep-19		575	22-Sep-19	3 Month Kibor +0.35%	10.79%	32	607	575
22-Dec-19		575	22-Dec-19	3 Month Kibor +0.35%	10.79%	16	591	-
		6,900				**1,663**	**8,563**	

Credit Rating Scale & Definitions

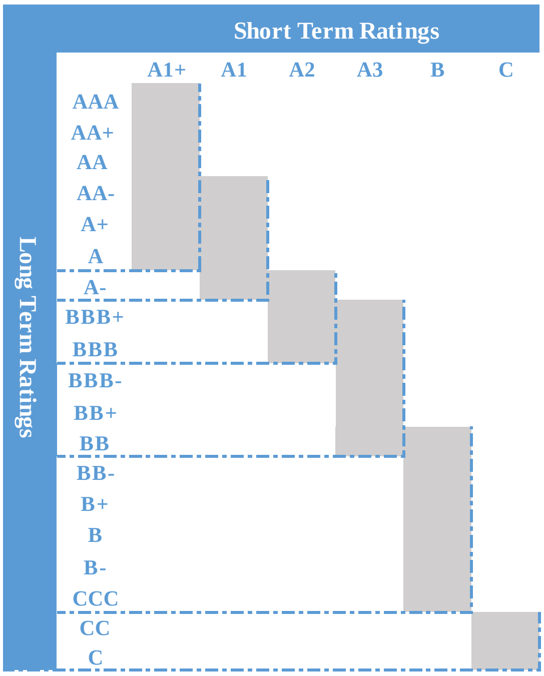
Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

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

Rating	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 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.

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

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

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(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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