RATING REPORT

Pakistan Telecommunication Company Limited

REPORT DATE:
October 14, 2021

RATING ANALYSTS:
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RATING DETAILS

Rating Category	Latest Rating		Previous Rating	
	Long-term	Short-term	Long-term	Short-term
Entity	AAA	A-1+	AAA	A-1+
Rating Date	*October 14, 2021*		*October 5, 2020*	
Rating Outlook	Stable		Stable	
Rating Action	Reaffirm		Reaffirm	

COMPANY INFORMATION

Incorporated in 1995	**External auditors:** KPMG Taseer & Hadi Co., Chartered Accountants.
Public Listed Company	
	President & CEO: Mr. Hatem Mohamed Bamatraf **Board of Directors:** - Dr. Muhammad Sohail Rajput (Chairman) - Abdulrahim A. Al Nooryani - Yusuf Khan - Hatem Dowidar - Hassan Nasir Jamy - Khalifa Al Shamsi - Syed Shabahat Ali Shah - Hesham Al Qassim - Dr. Mohamed Karim Bennis

APPLICABLE METHODOLOGY(IES)

VIS Entity Rating Criteria: Corporate Rating Methodology (August 2021)
https://docs.vis.com.pk/docs/CorporateMethodology202108.pdf

Pakistan Telecommunication Company Limited

OVERVIEW OF THE INSTITUTION

Pakistan Telecommunication Company Limited (PTCL) was incorporated in 1995 and provides telecommunication services in Pakistan through ownership of required facilities and infrastructure with reach expanding across the country.

PTCL was privatized in 2006 through sale of Class B shares. Etisalat International Pakistan (EIP), 90% owned subsidiary of Etisalat group, being the highest bidder acquired 26% stake in PTCL with the management control. Each Class B share has four voting rights for the purpose of election of directors. Majority shareholding remains with Government of Pakistan (GoP) which holds 62% of PTCL shares.

RATING RATIONALE

Pakistan Telecommunication Company Limited (PTCL) is the leading Integrated Information Communication Technology (ICT) Company in Pakistan, having the largest fixed-line network in the country. The company's products and services include voice services, high-speed broadband internet, Fiber to the Home (FTTH) services, CharJi wireless internet, Smart TV (IPTV) service, , Smart TV App and Touch App, digital-content streaming services like Netflix, and icflix, and enterprise-grade platforms like Smart Cloud, Tier-3 Certified Data Centers, Managed and Satellite Services.

Sector Dynamics

- Pakistan's teledensity has improved from 83% as of January 2021 to 86.8% as of August 2021. In terms of teledensity, Pakistan metrics are in line with regional counterparts. The country's cellular teledensity stands at 84.7%, while Fixed Local Loop (FLL) and Wireless Local Loop (WLL) teledensity stands at 2.14%, as of August 2021.
- The latest available data (August'2021) shows that total cellular, 3G/4G, and broadband subscribers have reached 186m, 103m and 106m respectively (July'20: 167m, 81m and 83m respectively). Meanwhile, basic telephony subscriber base has dropped from 3m to 2m.
- Given the contraction in revenue base, Average Revenue Per User (ARPU) per month for operators declined by 8% in FY20. The decline is noteworthy as Pakistan's ARPU was already trending at around half of South Asia average and a quarter of global average.
- The telecom sector is dominated by 4 Cellular Mobile Operators accounting for nearly four-fifth of the total telecom revenues. The remaining revenue is generated through Local Loop, Long Distance International (LDI), Wireless Local Loop (WLL) and Value-Added Services (VAS).
- Telecom sector revenue posted contraction during FY20, of about 2.4%, following 12.6% growth in the preceding period (FY20: Rs. 537b; FY19: Rs. 551b). The main reason for the contraction was the 4.8% drop in revenues from cellular services, which comprise 79% of the aggregate revenues; this is mainly on account of outright removal of 10% service, administrative and operation charges by operators on instructions of Supreme Court of Pakistan, besides the general trend of consumer shift toward VoIP services. The 2nd largest contributor Fixed Local Loop (FLL) and Wireless Local Loop (WLL) services, which comprise 15% of the aggregate, posted strong uptick of 13%.
- Following (net) FDI outflow of USD 78m in FY19, the sector recorded (net) FDI inflow of USD 623m in FY20.

Rating Drivers

Rating incorporates strong financial profile of sponsors and PTCL's market positioning

The assigned ratings take into account strong sponsor profile, as 62.2% shareholding is held by the Government of Pakistan (GoP) while 26% ownership and management control is held by Etisalat Group. Etisalat Group provides services to 149m subscribers globally and has expanded in 16 countries across the Middle East, Asia and Africa and is amongst the largest telecom operator in the world. The Group is rated AA- and Aa3 by S&P and Moody's, respectively.

The ratings also draw comfort from PTCL's leading market position in fixed-line voice, wire line broadband and wireless data segment.

Revenue base arises from 6 distinct segments; over the years 'Boradbad & FTTH' has emerged as the most dominant segment, while the traditional 'Voice Services' revenues have depicted contraction on a timeline

- **Broadband and FTTH:** Low cyclicality in sales and healthy demand outlook for Wireline broadband segment due to existing low penetration bodes well for revenue growth of the segment.
- **Voice:** Over the last few years, the traditional fixed line segment has witnessed customer erosion due to product substitution from CMOs and VoIP technologies, a trend VIS expects to continue. However, fixed line revenues from increasing broadband subscribers are expected to support revenues.
- **Wireless:** VIS expects overall industry revenues of the wireless segment to continue to decline given technology advances and ease & convenience of hot spot connectivity. In line with industry trend, PTCL's wireless segment revenues and customer base are expected to decline.
- **Corporate:** Segment has depicted healthy growth over the last 3 years where PTCL's diversified product offerings in the ICT segment (Amongst others these include Tier 3 Certified Data Centers hosting, Managed Services, Satellite Services, Smart Cloud, IT system integration projects, Managed Wifi solutions, Security and IP Surveillance Business) in addition to core connectivity business should continue to remain a growth driver. Growth has been particularly robust in revenues from cloud and data center services.
- **Wholesale & Carrier:** Growing demand for data is expected to bode well for revenues from the segment

Revenue base remained stagnant amidst a pandemic-induced slowdown in new customer acquisition, while margins have been impacted owing to changing consumer patterns during the pandemic.

PTCL has divided its operations into six segments; broadband & IPTV is the largest segment and accounts for 39% of total revenue, followed by carrier and wholesale 16%, voice service 15%, international 15%, , corporate 11% and wireless data 3%.

The company reported revenue of Rs. 71.8b (2019: Rs. 71.5b). The company's topline has remained restricted at a similar level during the past 3-year period (2018-2020). In 2020, the stagnation in topline is mainly attributable to absence of any growth in broadband & IPTV segment, given that new user acquisition was lower than expected, at 3%, while ARPU of the segment also declined by 3%. Healthy growth was noted the carrier & wholesale segment, which has become the 2nd largest segment, now contributing more than the voice services segment. On the contrary, voice services segment revenues contracted 14%, voice services segment users continue to decline, contracting by 2% in 2020. Growth in corporate segment revenues is largely contributed by growth services including data, data center, and cloud services. Overall revenues from the segment grew by 11%, as corporate reliance on data services increased as a result of the pandemic.

PTCL's gross margins took a hit during 2020, mainly as broadband usage tripled during the period, while ARPU contracted. Resultantly, gross margin contracted from 23.7% to 20.9%. PTCL reported operating profit of Rs. 3.4b during 2020 (2019: Rs. 4.3b), decline of which is attributable to subdued gross margin. Going forward, management projects EBITDA margins to recover due to focus on higher ARPU segments and value added services along with cost control initiatives.

During 1H'2021, PTCL reported strong improvement in revenue base, which grew by 8%, subsequent to posting stagnant topline performance in the past 3-year period (2018-2020). Healthy growth in revenues was noted in wireless data, corporate and broadband & IPTV segments. Given growth in higher ARPU segments, gross margins of the company improved to 22.8%.

PTCL also booked other income of Rs. 5.5b during 2020 (2019: Rs. 4.7b), which included gain on disposal of PPE (Rs. 1.4b), interest on loan to subsidiaries (Rs. 1.2b) and government grants recognized (Rs. 1.0b). Accounting for taxation, the company reported net profit of Rs. 6.0b

(2019: Rs. 6.3) and Rs. 3.7b during 2020 and 1H2021, respectively.

The ratings incorporate PTCL's strong balance sheet and abundant liquidity, elements that provide the company with financial flexibility and support its rating.

Liquidity position is strong, with significant cash resources available together with healthy cash flow generation. Assessment of PTCL's liquidity profile also incorporates favorable working capital cycle where consistent cash collection has resulted in no utilization of short-term borrowings and accumulation of liquidity buffer on balance sheet. Despite sizeable capital investments over the last three years, financial profile has remained comfortable with minimal debt on the balance sheet.

There is implied risk to PTCL by way of its holding of Ufone, given that Ufone is in losses and requires ongoing funding assistance. As of Sep'21, PTCL had extended Corporate Guarantees and Letters of Comfort to tune of Rs. 21b and Rs. 3.5b respectively. However, even after incorporating the same in PTCL's debt, the gearing ratio stands at 0.27, which is within the threshold. Going forward, there are plans for additional investment into Ufone in a two phases of Rs. 8b each in 2022 and 2023. This will be financed through a combination of bank financings and internal liquidity generation through sale of real estate assets available on the balance sheet. Incorporating the same, PTCL's gearing is projected to remain within threshold.

Sound Corporate Governance Framework

In accordance with the provisions of Share Purchase Agreement between GoP and Etisalat Group as well as under the Articles of Associations of PTCL, the GoP has four nominees while Etisalat Group has five nominees on the board. Management team comprises qualified personnel and is supported by a well-designed organization structure which has been made significantly leaner through 3 VSSs undertaken during the decade. PTCL has implemented a SAP based Enterprise Resource Planning system. Detailed and timely annual report disclosures bode well from a transparency perspective and provide important information to stakeholders.

FINANCIAL SUMMARY (Unconsolidated)

(amounts in PKR millions)

BALANCE SHEET	2015	2016	2017	2018	2019	2020	1H'2021
Fixed Assets	94,912	94,779	98,251	106,151	116,720	114,666	116,332
Trade Debts	14,304	14,228	16,040	16,658	20,259	23,150	25,009
Income Tax Recoverable	18,179	14,261	15,263	16,478	17,756	18,373	17,655
Short Term Investments	26,039	24,000	5,608	4,930	7	6,212	11,072
Cash & Bank Balances	2,210	5,902	14,243	4,661	4,168	5,764	5,435
Total Assets	180,378	182,637	186,158	196,523	209,994	223,600	231,816
Trade and Other Payables	46,814	59,143	62,003	67,675	78,262	88,457	92,246
Long Term Debt	-	-	-	-	-	-	-
Short Term Debt	-	-	-	-	-	-	-
Lease Liabilities	-	-	-	-	1,105	1,409	1,297
Total Debt	-	-	-	-	1,105	1,409	1,297
Paid up Capital	51,000	51,000	51,000	51,000	51,000	51,000	51,000
Total Equity	92,144	86,218	83,013	84,952	83,571	94,010	96,636

INCOME STATEMENT	2015	2016	2017	2018	2019	2020	1H'2021
Revenue	75,752	71,420	69,757	71,273	71,548	71,804	38,187
Gross Profit	21,968	21,062	18,714	17,742	16,979	14,997	8,693
Operating Profit	8,672	9,162	7,149	6,514	4,939	3,447	2,804
Adjusted EBITDA	26,603	26,145	24,204	26,519	26,359	26,359	14,294
Profit Before Tax	13,272	10,201	12,845	10,757	9,331	8,493	5,268
Profit After Tax	8,760	6,835	8,350	7,773	6,347	6,030	3,740

RATIO ANALYSIS	2015	2016	2017	2018	2019	2020	1H'2021
Gross Margin (%)	29%	29%	27%	25%	24%	21%	23%
Adjusted EBITDA Margin (%)	35%	37%	35%	37%	37%	37%	37%
Net Margin	12%	10%	12%	11%	9%	8%	10%
Trade debts/Sales	19%	20%	23%	23%	28%	32%	33%*
FFO	20,648	18,970	17,189	24,071	23,283	22,745	14,226
FFO to Total Debt (x)	NA	NA	NA	NA	21x	16x	22x
FFO to Long Term Debt (%)	NA	NA	NA	NA	21x	16x	22x
Current Ratio (x)	1.55	1.27	1.13	1.01	0.88	0.87	0.91
Debt Servicing Coverage Ratio (x)	NA	NA	NA	NA	NA	74x	94x
Gearing (x)	-	-	-	-	0.01	0.01	0.01
Leverage (x)	1.09	1.20	1.19	1.35	1.39	1.38	1.40
ROAA (%)	5%	4%	5%	4%	3%	1%	3%*
ROAE (%)	10%	8%	10%	9%	7%	3%	8%*

** Ratios Annualized*

ISSUE/ISSUER RATING SCALE & DEFINITIONS Appendix II

VIS Credit Rating Company Limited

RATING SCALE & DEFINITIONS: ISSUES / ISSUERS

Medium to Long-Term

AAA
Highest credit quality; the risk factors are negligible, being only slightly more than for risk-free Government of Pakistan's debt.

AA+, AA, AA-
High credit quality; Protection factors are strong. Risk is modest but may vary slightly from time to time because of economic conditions.

A+, A, A-
Good credit quality; Protection factors are adequate. Risk factors may vary with possible changes in the economy.

BBB+, BBB, BBB-
Adequate credit quality; Protection factors are reasonable and sufficient. Risk factors are considered variable if changes occur in the economy.

BB+, BB, BB-
Obligations deemed likely to be met. Protection factors are capable of weakening if changes occur in the economy. Overall quality may move up or down frequently within this category.

B+, B, B-
Obligations deemed less likely to be met. Protection factors are capable of fluctuating widely if changes occur in the economy. Overall quality may move up or down frequently within this category or into higher or lower rating grade.

CCC
Considerable uncertainty exists towards meeting the obligations. Protection factors are scarce and risk may be substantial.

CC
A high default risk

C
A very high default risk

D
Defaulted obligations

Short-Term

A-1+
Highest certainty of timely payment; Short-term liquidity, including internal operating factors and /or access to alternative sources of funds, is outstanding and safety is just below risk free Government of Pakistan's short-term obligations.

A-1
High certainty of timely payment; Liquidity factors are excellent and supported by good fundamental protection factors. Risk factors are minor.

A-2
Good certainty of timely payment. Liquidity factors and company fundamentals are sound. Access to capital markets is good. Risk factors are small.

A-3
Satisfactory liquidity and other protection factors qualify entities / issues as to investment grade. Risk factors are larger and subject to more variation. Nevertheless, timely payment is expected.

B
Speculative investment characteristics; Liquidity may not be sufficient to ensure timely payment of obligations.

C
Capacity for timely payment of obligations is doubtful.

Rating Watch: VIS places entities and issues on 'Rating Watch' when it deems that there are conditions present that necessitate re-evaluation of the assigned rating(s). Refer to our 'Criteria for Rating Watch' for details. www.vis.com.pk/images/criteria_watch.pdf

Rating Outlooks: The three outlooks 'Positive', 'Stable' and 'Negative' qualify the potential direction of the assigned rating(s). An outlook is not necessarily a precursor of a rating change. Refer to our 'Criteria for Rating Outlook' for details.www.vis.com.pk/images/criteria_outlook.pdf

(SO) Rating: A suffix (SO) is added to the ratings of 'structured' securities where the servicing of debt and related obligations is backed by some sort of financial assets and/or credit support from a third party to the transaction. The suffix (SO), abbreviated for 'structured obligation', denotes that the rating has been achieved on grounds of the structure backing the transaction that enhanced the credit quality of the securities and not on the basis of the credit quality of the issuing entity alone.

(blr) Rating: A suffix (blr) is added to the ratings of a particular banking facility obtained by the borrower from a financial institution. The suffix (blr), abbreviated for 'bank loan rating' denotes that the rating is based on the credit quality of the entity and security structure of the facility.

'p' Rating: A 'p' rating is assigned to entities, where the management has not requested a rating, however, agrees to provide informational support. A 'p' rating is shown with a 'p' subscript and is publicly disclosed. It is not modified by a plus (+) or a minus (-) sign which indicates relative standing within a rating category. Outlook is not assigned to these ratings. Refer to our 'Policy for Private Ratings' for details. www.vis.com.pk/images/policy_ratings.pdf

'SD' Rating: An 'SD' rating is assigned when VIS believes that the ratee has selectively defaulted on a specific issue or obligation but it will continue to meet its payment obligations on other issues or obligations in a timely manner.

REGULATORY DISCLOSURES — Appendix III

Name of Rated Entity	Pakistan Telecommunication Company Limited
Sector	Telecommunication Industry
Type of Relationship	Solicited
Purpose of Rating	Entity Rating

Rating History

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
	RATING TYPE: ENTITY			
October 14, 2021	AAA	A-1+	Stable	Reaffirmed
October 5, 2020	AAA	A-1+	Stable	Reaffirmed
October 11, 2019	AAA	A-1+	Stable	Reaffirmed
October 11, 2018	AAA	A-1+	Stable	Initial

Statement by the Rating Team
VIS, the analysts involved in the rating process and members of its rating committee do not have any conflict of interest relating to the credit rating(s) mentioned herein. This rating is an opinion on credit quality only and is not a recommendation to buy or sell any securities.

Probability of Default
VIS' ratings opinions express ordinal ranking of risk, from strongest to weakest, within a universe of credit risk. Ratings are not intended as guarantees of credit quality or as exact measures of the probability that a particular issuer or particular debt issue will default.

Disclaimer
Information herein was obtained from sources believed to be accurate and reliable; however, VIS does not guarantee the accuracy, adequacy or completeness of any information and is not responsible for any errors or omissions or for the results obtained from the use of such information. . For conducting this assignment, analyst did not deem necessary to contact external auditors or creditors given the unqualified nature of audited accounts and diversified creditor profile.

Due Diligence Meetings Conducted

Name	Designation	Date
Mr. Amir Siddiqui	EVP- Group FP&T	22-Sept-2021
Mr. Abdullah Rafique	GM Billing & BI Reporting	22-Sept-2021