RATING REPORT

Digital World Pakistan (Pvt.) Limited

REPORT DATE:
March 04, 2019

RATING ANALYSTS:
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RATING DETAILS		
Rating Category	**Initial Rating**	
	Long-term	**Short-term**
Entity	A-	A-2
Rating Outlook	*Stable*	
Rating Action	Initial	
Rating Date	*February 28, '19*	

COMPANY INFORMATION	
Incorporated in 2000	External Auditors: Sarwars Chartered Accountants
Private Limited Company	Chairman/CEO: Mr. Muhammad Farooq Naseem
Key Shareholders (with stake 5% or more):	
Mr. Farooq Naseem – 46%	
Mr. Taha Muhammad Naseem – 18%	
Mr. Zaka Muhammad Naseem – 10%	
Mrs. Roohi Farooq Naseem – 8%	
Mr. Aftab A. Tapal – 6%	

APPLICABLE METHODOLOGY(IES)
VIS Entity Rating Criteria: Industrial Corporates (May 2016)
https://www.vis.com.pk/kc-meth.aspx

Digital World Pakistan (Pvt.) Limited

OVERVIEW OF THE INSTITUTION

Digital World Pakistan (Pvt.) Limited (DWPL) was incorporated in 2000 as a private limited company under the repealed Companies Ordinance, 1984 (now the Companies Act, 2017). The company is engaged in manufacturing and sale of consumer electronic products.

Profile of the Chairman/CEO

Mr. Farooq Naseem is the founder of DWPL. He serves the company as Chairman of the Board and Chief Executive Officer. Mr. Farooq has over 20 years of experience in Electronics, Information Technology, Textile and Agro Industries.

Financial Snapshot

Tier-I Equity: end-1HFY19: Rs. 2.0b; end-FY18: Rs. 1.9b; end-FY17: Rs. 1.6b.

Assets: end-1HFY19: Rs. 6.4b; end-FY18: Rs. 8.3b; end-FY17: Rs 6.5b.

Profit After Tax: 1HFY19: Rs. 72m; FY18: Rs. 368m; FY17: Rs. 339m.

RATING RATIONALE

Digital World Pakistan (Pvt.) Limited (DWPL) is an assembler of renowned consumer durable brands. The company is a part of DWP Group and is majority owned by the sponsoring family. The assigned ratings take into account sponsors' industry experience, particularly in the end-to-end supply chain management. The business risk profile of DWPL is underpinned by positive dynamics of consumer durables industry, strong brand equity in air conditioner and LED television categories and established business relations with the vendors and dealers. The ratings also incorporate recent augmentation of production capabilities, consistent upgradation of product lines, and aggressive marketing spending, resulting in enhanced sales.

The ratings are constrained by significant dependence on distribution rights of Gree-branded products, dynamic consumer preferences for consumer durable goods, high price sensitivity and vulnerability to foreign exchange risk. The ratings also factor in comparatively low profit margins, slightly higher debt leverage indicators, and weak corporate governance framework. The ratings will remain sensitive to the maintenance of strategic relations with Gree Electric Appliances Inc. and consistency in profit margins and leverage indicators.

Rating Drivers

Sales and Profitability

DWPL registered 15% growth in net sales during FY18, driven largely by higher volumetric sales and favorable prices. Gross margin increased slightly during FY18 mainly on account of favorable selling prices. Franchise value of its products along with bargaining power with supplier have helped the company to sustain gross margins. The management is anticipating some pressure on margins during FY19 due to rupee depreciation. With higher spending on advertising and sales promotion, distribution & selling expenses stood higher during FY18. The slight increase in finance cost was due to higher utilization of running finance. Despite higher effective tax expenses, DWPL registered 8% increase in net profits during FY18. Net sales and profit after tax were recorded lower during 1HFY19, mainly on account of seasonality related to air conditioner business.

Liquidity & Cash Flow

Liquidity position of the company remained at adequate levels despite some decrease in current ratio by end-FY18. The current ratio improved during 1HFY19 on the back of significant reduction in short-term borrowings. DWPL registered healthy growth in funds from operations (FFO) during FY18 on the back of higher profits. FFO during FY17 were negatively impacted by a one-off tax payment. Due to higher cash flows generation and modest long-term debt balance, FFO to long-term debt ratio was recorded higher at end-FY18. Similarly, the debt service coverage ratio stood higher at end-FY18. During 1HFY19, cash flow coverages do not provide a holistic picture due to the seasonality impact.

Capitalization and Funding

Core equity base of the company augmented further by end-1HFY19 with the continued accumulation of profits. The debt profile is largely composed of short-term borrowings, with a nominal portion of long-term financing. Short-term borrowings included finance against trust receipt, running finance facility and letter of credit against which the company recognizes stock in transit. Outstanding balance of long-term debt decreased with the scheduled repayments. DWPL is in the process of mobilizing long-term borrowings during FY19 for the procurement of heat exchanger.

DWPL uses a mix of short-term borrowings and USD denominated open account credit facilities from the suppliers to meet its working capital requirements. The company increased utilization of open account credit during 1HFY19, resulting in significantly lower short-term borrowings. Whereas, trade & other payables were recorded higher owing to shift towards supplier credit during 1HFY19. With the reduction in short-term borrowings and increase in equity, gearing and debt leverage indicators improved by end-1HFY19.

Industry Dynamics and Future Outlook

Demand within the consumer durable industry is mainly a function of population growth, GDP per capita, urbanization, changing demographic distribution and growing awareness with trends of technology. Since 2000, population in Pakistan has grown at a rate of 2.4% p.a., while GDP per capita increased to $1,468 (FY16: $1,426) during FY17. Proportion of middle income population has grown to 45% in 2015 as compared to 33% in 2001; the same is projected to increase, going forward.

Moreover, speedy urbanization, higher influx of younger people in the demographic, improved standard of living and greater awareness with new technological trends have and will further translate into healthy demand for consumer durables in Pakistan as they have become a necessity rather than a luxury.

Digital World Pakistan (Pvt.) Limited **Annexure I**

FINANCIAL SUMMARY *(amounts in PKR millions)*				
BALANCE SHEET	**FY16**	**FY17**	**FY18**	**1HFY19**
Non-Current Assets	683	948	1,174	1,144
Stock in Trade	1,460	2,919	3,448	3,096
Trade Debts	137	160	274	335
Other Current Assets	474	952	1,743	1,360
Cash and Bank Balance	726	1,491	1,615	489
Total Assets	**3,480**	**6,470**	**8,254**	**6,424**
Trade and Other Payables	899	2,763	1,419	2,538
Short Term Borrowings	825	1,618	4,411	1,571
Long-Term Borrowings *(Inc. current matur)*	173	58	49	36
Other Liabilities	214	233	381	214
Total Liabilities	**2,111**	**4,762**	**6,260**	**4,359**
Tier-1 Equity	**1,211**	**1,559**	**1,853**	**1,928**
Total Equity	1,368	1,707	1,994	2,066
INCOME STATEMENT	**FY16**	**FY17**	**FY18**	**1HFY19**
Net Sales	7,751	11,190	12,858	3,531
Gross Profit	1,211	1,769	2,080	554
Operating Profit	398	589	676	129
Profit After Tax	226	339	368	72
FFO	254	55	529	96
RATIO ANALYSIS	**FY16**	**FY17**	**FY18**	**1HFY19**
Gross Margin (%)	15.6	15.8	16.2	15.7
Net Working Capital	896	956	1,032	1,124
FFO to Long-Term Debt (x)	1.47	0.94	10.81	5.25*
FFO to Total Debt (x)	0.25	0.03	0.12	0.06*
Debt Servicing Coverage Ratio (x)	3.59	1.38	9.24	4.31
ROAA (%)	-	6.8	5.0	2.0*
ROAE (%)	-	24.5	21.6	7.6*
Gearing (x)	0.82	1.08	2.41	0.83
Adjusted Gearing (x)**	0.26	0.13	1.67	0.63
Debt Leverage (x)	2.00	3.39	3.69	2.46
Adjusted Debt Leverage (x)**	1.31	2.33	2.74	2.18
Inventory + Receivable/Short-term Borrowings (x)	1.94	1.90	0.84	2.18
Current Ratio (x)	1.47	1.21	1.17	1.27

**Annualized*

*** Adjusted for cash and irrecoverable amount related to Samsung*

ISSUE/ISSUER RATING SCALE & DEFINITIONS Annexure 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	Annexure III
Name of Rated Entity	Digital World Pakistan (Pvt.) Limited
Sector	Consumer Appliances
Type of Relationship	Solicited
Purpose of Rating	Entity Ratings
Rating History	see table below
Instrument Structure	N/A
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.
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Rating History

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
RATING TYPE: ENTITY				
28/02/2019	A-	A-2	Stable	Initial