RATING REPORT

Transsion Tecno Electronics (Pvt) Limited

REPORT DATE:
June 16, 2023

RATING ANALYSTS:
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RATING DETAILS				
	Latest Rating		Previous Rating	
Rating Category	**Long-term**	**Short-term**	**Long-term**	**Short-term**
Entity Rating	BBB+	A-2	BBB+	A-2
Rating Date	*June 16, '23*		*April 13, '23*	
Rating Outlook	Stable		Rating Watch - Developing	
Rating Action	Maintained		Maintained	

COMPANY INFORMATION	
Incorporated in 2019	**External Auditors:** Rao & Company Chartered Accountants
Private Limited Company	**Chairman:** Mr. Iqbal Ahmed Allawala **Chief Executive Officer:** Mr. Asif Allawala
Key Shareholders (with stake 5% or more):	
Tecno Pack Telecom (Private) Limited – 60% Transsion Technology Limited – 40%	

APPLICABLE METHODOLOGY(IES)

Applicable Rating Criteria: Corporates (May 2023):
https://docs.vis.com.pk/docs/CorporateMethodology.pdf

APPLICABLE RATING SCALE(S)

VIS Issue/Issuer Rating Scale:
https://docs.vis.com.pk/docs/VISRatingScales.pdf

Transsion Tecno Electronics (Pvt) Limited

OVERVIEW OF THE INSTITUTION

Transsion Tecno Electronics is a private limited company incorporated in 2019. The Company is one of the leading smartphone assemblers in Pakistan. The Company has three brands in their smart phones category.

Profile of CEO

Mr. Asif Allawala is the CEO of the Company since the incorporation. He is working with Tecno group since 1994. He is also a Director and CEO of other group companies. He has secured a Masters of Business Administration (MBA) degree from United States of America (USA)

RATING RATIONALE

Transsion Tecno Electronics (Private) Limited (TTE) is principally engaged in the assembly of mobile phones under three different brands, namely, **Infinix, Tecno and Itel**, to cater local and international demand. The Company belongs to the **Tecno Group** which has exposure in the automobile parts and electronic goods industries. Other group entities include Tecno Auto Glass Ltd (joint venture with Pak Suzuki Motor Co.), Tecno Pack Electronics (Pvt) Ltd. and Tecno Pack Telecom.

TTE is essentially a joint venture between Tecno Pack Telecom (The Holding Company) and Transsion Technology Limited, a world-leading Chinese mobile manufacturing firm. The Company's production facilities include 2 factories with a total of 11 assembly lines that have an annual production capacity of about 5 million units. The plants are located at Korangi Industrial Area, Karachi while the corporate office is situated at PECHS, Karachi.

Elevation of business risk as import restrictions resulted in plant closure in 3QFY23, however, gradual opening of LCs has resulted in resumption of operations in May'23

TTE's business model entails receiving semi-knocked down (SKD)/completely-knocked down (CKD) mobile kits from Transsion Technology in China and assembling them locally for a fixed USD-denominated fee, ensuring a partial inflationary hedge. The Company is not required to pay for any marketing, selling or financing costs nor does it need to undertake raw material procurement, which are the responsibilities of Transsion Technology. Moreover, TTE receives advance payments from customers which are backed by inventory and advances to suppliers. These deliveries also have pre-defined lead times which is about 40 days from receipt of advance. The Company's current contract with Transsion Technology is valid till 2029 and requires compliance with pre-defined benchmarks.

The local mobile manufacturing industry received a major boost in recent years due to the Mobile Device Manufacturing Policy (MDMP) which was instituted to encourage localization of assembly processes for mobile phones. Additionally, ongoing import restrictions, high duties and severe currency devaluation have also discouraged purchase of imported phones, resulting in locally assembled/manufactured phones dominating about 93.3% of the domestic market in 2022. Despite rising prices, future demand outlook is expected to be positive given the country's rising youth population as well as expansion of cellular subscribers which have risen with a CAGR of 5.1% over the last five years. The local industry consists primarily of Chinese brands including Xiomi, Oppo, and VIVO as well as TTE but high-end brands such as Samsung and Nokia have also setup plants in the country. The Company primarily targets the lower to middle income market segment where price competition is significant owing to the high price-sensitivity of consumers, especially given the unprecedented levels of inflation during the ongoing year, as well as presence of several other inexpensive Chinese brands in the market. TTE, however, dominates the local industry with a cumulative overall market share of about 25% in quantitative terms across its three brand offerings.

On the supply-side front, the Company faced significant challenges due to import restrictions imposed by the Government to manage foreign exchange depletion. The firm closed operations in March'23 owing to lack of raw material availability during which fixed overhead expenses were partially covered by profit bearing deposits. As per management, production resumed during May'23 as the Company was able to open import LCs.

Growth in topline during FY22 was followed by sharp decline in ongoing year owing to lack of raw materials, however, uptick in margins witnessed attributable to inventory gains

Net sales grew by 22.8% during FY22 despite a slight decline in quantum sold by 1.9% as average prices rose by 25.2%. Sales mix was dominated by the Infinix brand which constituted about 55.1% of net sales (FY21: 56.2%) followed by Tecno at 37% (FY21: 35.5%) and Itel at 7.8% (FY21: 8.3%). In terms of geographical sales mix, a shift was witnessed towards the Central region which generated 42% of net sales while the South and North regions stood at 35% and 23%, respectively (FY21: 36%, 33%). The Company supplies its products across 27 distributors, as per agreements with Transsion Technology, with the top 10 customers constituting about 90.6% of the topline in 11MFY23 (FY22: 90.5%, FY21: 97.5%). While notable client concentration is exhibited, the associated risk is considered minimal given that TTE is not responsible for marketing or selling operations.

Gross margins squeezed to 1.3% (FY21: 3.4%) in the outgoing year as higher costs were not fully passed on to customers. Net margin also decreased to 0.6% (FY21: 1.7%) largely on the account of rise in administrative costs due to higher salary expenses and directors' remuneration. Also, higher financing costs in line with hike in policy rates as well as increase in other expenses owing to exchange losses added further pressure on margins.

During 10MFY23, topline decreased sharply by 59.2% on an annualized basis on the back of raw material constraints and plant closure during several months. However, gross margin increased notably to 9.8% due to inventory gains as higher costs were fully passed on to customers amidst an import restricted environment. Net margins, albeit higher vis-à-vis FY22, stood at a meager 1.8% as significant exchange losses dragged overall profitability levels. According to management, operations have resumed during May'23 with the opening of LCs of completely knocked-down (CKD)/semi-knocked down (SKD) mobile kits, the amount of which is about 82% of average monthly sales (July'22). Going forward, the management expects to meet its monthly sales target beginning from July'23 and forecasts total unit sales for FY24 to be slightly higher than FY22 levels. Materialization of the projected plans will be important.

Sufficient liquidity profile following the advance from customers model

The company's Funds from Operations (FFO), while comparatively better than FY22 due to higher margins, was reported on the lower side in comparison to FY21 levels. FFO-to-total debt and debt-service coverage were both adequate at 5.65x (FY22: 3.42, FY21: 10.28x) and 16.47x, respectively (FY22: 6.9x; FY21: 59.5x) in 10MFY23. Maintaining the same over the rating horizon will be critical.

Stock levels for April end do not depict an accurate reflection as LCs were in transit. Current ratio of the Company was reported adequately at 1.59x (FY22: 1.25x, FY21: 1.05x) at end-April'23. Reliance on advance payments from customers eliminates the need for trade debts, contributing to a low net operating cycle. This model therefore supports the capitalization profile of the Company given no requirement of short-term borrowings.

Low gearing levels owing to minimal debt levels given absence of short-term borrowings

The equity base continued an upward trend at end-April'23 on account of profit retention. The company's total debt levels remained minimal, consisting exclusively of long-term lease liabilities. Short-term borrowings are not required as the proceeds from advance payments are utilized to meet working capital requirements. Consequently, gearing levels are on the lower side standing at 0.11x (FY22: 0.19x, FY21: 0.24x) at end-April'23. Leverage, on the other hand, is relatively elevated owing to advance payments from customers but the same is matched by inventory and advances to suppliers, reducing risk exposure.

REGULATORY DISCLOSURES	Appendix I
Name of Rated Entity	Transsion Tecno Electronics (Pvt) Limited
Sector	Mobile Phones
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				
16-June-23	BBB+	A-2	Stable	Maintained
13-April-23	BBB+	A-2	Rating Watch – Developing	Maintained
29-Aug-22	BBB+	A-2	Stable	Initial

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.
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Due Diligence Meetings Conducted	

Name	Designation	Date
Jamil Ahmed	CFO	June 04, 2023