RATING REPORT

Tech Sirat (Private) Limited (TSPL)

REPORT DATE:
22nd Feb, 2024

RATING ANALYSTS:

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RATING DETAILS		
Rating Category	**Initial Rating**	
	Long-term	**Short-term**
Entity	BBB+	A-2
Rating Outlook	*Stable*	
Rating Action	Initial	
Rating Date	*Feb 22nd , 2024*	

COMPANY INFORMATION	
Incorporated in 2014	**External auditors:** Mazars M.F & Co. Chartered Accountants.
Private Limited Company	CEO: Mr. Kamran Nishat
Key Shareholders (with stake 5% or more): M/S Muller & Phipps Pakistan (Private) Limited – 99.99%	

APPLICABLE METHODOLOGY(IES)
VIS Entity Rating Criteria: Corporates (May 2023) **https://docs.vis.com.pk/docs/CorporateMethodology.pdf**
VIS Rating scale (2023) **https://docs.vis.com.pk/docs/VISRatingScales.pdf**

Tech Sirat (Private) Limited

OVERVIEW OF THE INSTITUTION

Tech Sirat (Private) Limited was incorporated in 2014. The firm is principally engaged in the distribution of mobile phones and laptops. The registered office is located at Dean arcade, main Clifton road, Karachi.

RATING RATIONALE

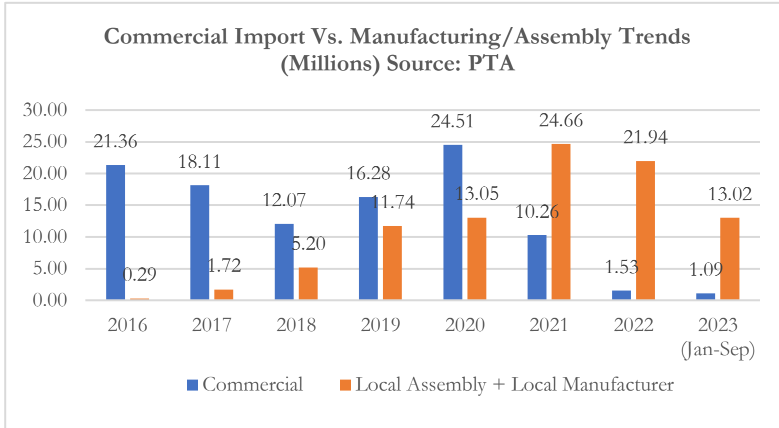
Tech Sirat (Private) Limited (TSPL) was incorporated on March 25, 2014, in Pakistan under the Companies Ordinance 1984 (now Companies Act, 2017). The Company is a subsidiary of M/s. Muller and Phipps Pakistan (Private) Limited (Parent company) which holds 99.99% shareholding. Muller & Phipps Pakistan Private Ltd. (M&P) has a long-established operating history of more than a century in logistic & distribution business. The Company is mainly engaged in import and supply of smart phones and computers. TSPL has a wholly owned subsidiary, namely Tech Sirat Technologies (Private) Limited (the Subsidiary) in which the Company holds 99.99% shareholding. The board of directors of TSPL is entirely composed of members from its Parent Company's Board /Management.

Key Rating Drivers

Industry Overview: As of Sept 2023, the smartphone industry in Pakistan boasts a substantial number of active cellular subscribers amounting to 190 million and 127 million mobile broadband users, showcasing a mobile teledensity of 79.44% and mobile broadband penetration of 53.14%, as reported by the Pakistan Telecommunication Authority (PTA). The PTA continues to implement the Device Identification Registration Blocking System (DIRBS), initiated in 2019, to curb the trade of illegal, substandard, and stolen mobile devices, thus ensuring a regulated market. In 2020, the Government of Pakistan (GOP) unveiled a comprehensive mobile manufacturing policy to promote local manufacturing, focused on incentivizing local assemblers by providing jobs to the skilled and semi-skilled workforce. This policy enabled assemblers to import semi-knocked down (SKD) units and assemble them in Pakistan while paying negligible duties and taxes. During the same year, the Engineering Development Board (EDB) also organized a mobile manufacturing summit to provide a roadmap for industry development, with 31 local manufacturers receiving Mobile Device Manufacturing (MDM) authorization to partake in this initiative.

Meanwhile, the Pakistani mobile phone assembly industry faced a severe crisis in early 2023 when nearly all of its 30 assembly units, including three operated by foreign brands, ceased operations due to import restrictions amid dollar shortage that resulted in critical shortages of raw materials. This crisis put approximately 20,000 jobs at stake as most companies temporarily furloughed their workforce. The Pakistan Mobile Phone Manufacturers Association (PMPMA) urgently appealed to the government to permit the import of parts in reasonable quantities to enable the industry to operate at half capacity, thereby mitigating the immediate impact of this crisis on the sector.

Despite these challenges, in February 2023, 2.35 million mobile phones were manufactured compared to 0.19 million imported commercially, according to sources. Mobile phone imports registered a MoM decline of 36.4%, amounting to $33.05 million. In late June'23, SBP reserves showed some increase mainly due to receipt of GoP inflows. Subsequently, SBP has relaxed import restrictions by abolishing criteria for essential and non-essential imports, particularly to help the industries that largely depend on imported raw materials. According to PTA, during Jan-Sep'23, locally manufactured/assembled mobile phones amounted to 13.02 million as compared to commercially imported 1.09 million. Whereas in Jan-Dec'22, locally manufactured mobile phones were reported at 21.84 million units vis-à-vis 1.53 million commercially imported. The distributors play an indispensable role in channeling mobile phones from manufacturers to retailers and wholesalers, while also offering essential after-sales services and official warranties. In March 2022, Airlink Communication Limited, partnering with Xiaomi, inaugurated the Mobile Device Manufacturing (MDM) facility for the production of Xiaomi's handsets in Pakistan. Xiaomi remains a notable player in the Pakistani smartphone market, especially within the budget phone category. Although the company may not prioritize the sale of high-end phones in the country, its impact is strongly experienced by consumers mindful of budget considerations. A comparison of commercial import vs. local manufacturing/assembly trend over the years is presented as follows:



According to Mobile Vendor, market share data for Pakistan for the Month of October 2023, presented by *Stat counter Global Stats*, Xiaomi is among top brands sold in the country with 6.6% market share. The other top brands include Samsung (17.92%), Vivo (13.89%), Infinix (13.67%), Oppo (13.34%) and Tecno (8.6%). The mobile phone industry in Pakistan exhibits resilience and potential, yet the challenges faced in the ongoing year highlight the need for supportive governmental policies and a robust framework. With favorable policies, eased import regulations, and incentivized local manufacturing, the industry could better harness its potential, fostering innovation and contributing more significantly to the national economy.

Strong Sponsor's Profile: The Company is a wholly owned subsidiary of Muller & Phipps Pakistan (Private) Limited ("M&P" or "the Company") that has a long-established operating history of more than a century in logistic & distribution business. The Company as a leading national distribution player provides pan Pakistan logistics & distribution, cold chain warehousing, sales, marketing and after sales support services. M&P has a robust and diversified principal base with 61 principals segmented into four distinct business divisions including Pharmaceutical, Telecommunication, Consumer & Allied and Healthcare. The Company is rated by VIS, with respective long-term and short-term ratings of A+ and A-1, indicating good credit quality with high certainty of timely payments. Total asset base of M&P was recorded at Rs.41.3b as of Mar 31, 2023.

Distribution Agreements: TSPL is one of the leading distributors of mobile phones, and other technology products in Pakistan. TSPL partnered with Xiaomi (the Principal) in November 2016 and is among the five-official partners in Pakistan, leading majority of Xiaomi's local presence. Other distributors include Airlink Technologies, Smart-link Technologies, and Phonezo. TSPL has also partnered with Lenovo PC HK Limited to fulfil laptop orders for different corporates by having in place an exclusive partnership agreement. In addition to this, ASUS Global Pte. Ltd., a Singapore based technology company, known for developing high end gaming laptops, has also inked an agreement with TSPL to help it enter the local gaming market.

The company houses an internal audit department which ensures compliance with regulations and evaluates internal controls.

Revenue & Profitability: Xiaomi has direct competition with Infinix, Tecno and ITEL in terms of comparative price range offered by these brands as all of these are largely skewed towards mass market in Pakistan. In view of M&P's leading market position in distribution industry, Xiaomi has notably increased its reliance on TSPL. During 10M'CY23, net sales were recorded at Rs.7.8b (CY22: Rs. 6.4b). During the same period, ~96 of the revenue emanated from sale of mobile phones of Xiaomi Pakistan (Pvt.) Ltd., while the remaining was contributed from Lenovo PC sales. Whereas in CY22, laptop sales accounted for ~22% of the revenue mix. During 10M'CY23, the company sold almost 207K (CY22: 149.9K) mobile units at an average price of Rs. 35,873/ unit (CY22: Rs. 34,264). The sales of Lenovo laptops are majorly linked to the demand by corporates, which fluctuates time and off. TSPL sells mobile phones to local dealers, whereas Lenovo PC sales are directed towards corporate clientele. The lead time for delivery of mobile handsets is around 30 days, while the average timeline for sale of products after delivery is 2-3 days. Monthly sales data showed subdued sales in Feb to Jun, 2023 on account of obstruction in local manufacturing of phones due to supply chain issues related to LC establishment, as discussed earlier in this report. Subsequent to improvement in forex reserves in June, 2023 and SBP's relaxation on opening of LCs, Xiaomi resumed manufacturing mobile phones locally. Resultantly, the revenue figures started recovering, with major growth witnessed in August, 2023 with an onwards trend following. The volumetric sales are directly linked to the local production volumes, along with sales targets given from the principal while TSPL avails fixed distribution margins as agreed with the Principal. The distribution agreement not only ensures that TSPL is fully compensated for the discounts on products but also provides indemnification for any loss of sales related to older models that could not be sold due to the introduction of new ones.

Going forward, in line with some recovery in economic conditions, TSPL expects to close topline for CY23, at Rs. 10.5b while gross margins are expected to remain around similar levels. Finance cost during CY23 is expected to increase more than two-folds vis-à-vis previous year on account of sizable short-term borrowings coupled with higher markup rates. As per the management, CY24 is expected to bolster topline with approximately 50% growth on YoY basis; however, gross margins are projected to remain largely stable. In the medium-to-long term, on account of available group synergies, TSPL intends to add a few other distributions in its portfolio as well.

Liquidity Profile: TSPL's working capital requirements primarily stem from financing inventory purchases, which typically involve making advance payments to the Principal, with a standard duration of thirty days. As of Oct'23, advances, deposits, prepayments, and other receivables were recorded higher largely due to higher advance payments made to the Principal against inventory purchase, reimbursements associated with discounts and marketing expenses executed on behalf of the Principal. Additionally, the surge was attributed to a higher outstanding margin amount related to importing laptops through LC. Resultantly, short-term borrowings increased substantially by end-Oct'23 leading to drop in cash flow coverages. Nonetheless, cash flow coverages have remained largely adequate in relation to outstanding obligations, on a timeline basis. The liquidity position of the company is also supported by its Parent Company, as required.

Trade debts (although unsecured) were recorded lower due to shift in credit policy. Trade debts have remained very limited as a percentage of net sales as majority sales of mobile phones are on cash or advance payments. However, in laptops/computer business, the credit period ranges between 30 to 40 days. Ageing profile of unimpaired receivables is considered satisfactory as majority fall due in one to three months credit bracket. Trade and other payables have increased, which majorly included trade creditors. Improvement in working capital management and maintaining adequate cash flow coverages are considered imperative from ratings purview.

Capitalization: The paid-up capital of TSPL amounted to Rs. 120m (CY22: Rs. 120m). The growth in tier-1 equity has been driven by profit retention over the years (10M'CY23: Rs. 621.2m; CY22: Rs. 460.5m).

The debt profile of TSPL comprises majorly of short-term borrowings. The long-term lease liabilities, i.e. Right-of-Use Assets (including current portion) have been obtained against lease contracts for the depots. These leases generally have lease terms from 1 to 3 years. According to management, going forward, the Company anticipates a decrease in leverage indicators as it is actively working to reduce its working capital needs amid higher interest rates.

Tech Sirat (Private) Limited Annexure I

FINANCIAL SUMMARY *(amounts in PKR millions)*				
BALANCE SHEET	**CY20**	**CY21**	**CY22**	**10M'CY23**
Paid-Up Capital	**120**	**120**	**120**	**120**
Total Equity	**72.6**	**323.9**	**460.5**	**621.2**
INCOME STATEMENT	**CY20**	**CY21**	**CY22**	**10M'CY23**
Net Sales	7,751.70	7,824.90	6,393.20	7,774.40
Profit Before Tax	410.6	484.2	275.1	302.3
Profit After Tax	236.1	250.5	135.5	160.7
RATIO ANALYSIS	**CY20**	**CY21**	**CY22**	**10M'CY23**
Current Ratio (x)	1.08	1.4	1.7	1.17
Gearing (x)	0.49	0.2	0.06	2.32

Annualized

REGULATORY DISCLOSURES — Annexure IV

Name of Rated Entity	Tech Sirat (Private) Limited
Sector	Miscellaneous Non-Manufacturing
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				
22-Feb-24	BBB+	A-2	Stable	Initial

Due Diligence Meetings Conducted

Name	Designation	Date
Mr. Faizan Malik	Finance Manager	Sept 15, 2023
Mr. Mubashir Hassan	Accounts Manager	Sept 15, 2023