

VIS

Credit Rating Company Limited

HOUSEHOLD APPLIANCES

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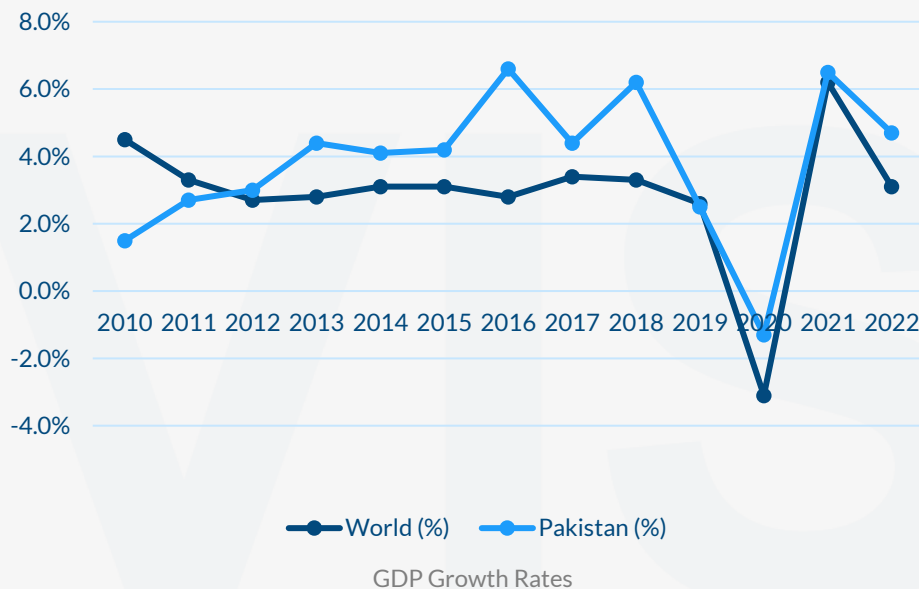
INTRODUCTION

The household appliances sector is integral to consumers' daily lives, offering tools to enhance domestic efficiency and convenience. Household appliances can be broadly categorized into major and minor segments. Major appliances, encompassing durable goods such as refrigerators, washing machines, and cooking appliances, are vital for the fundamental functionalities of a modern household. On the other hand, minor appliances, comprising smaller devices like toasters, blenders, and vacuum cleaners, contribute to the overall comfort and ease of domestic tasks.

ECONOMIC OVERVIEW

GLOBAL

The global economy faces subdued growth amid heightened uncertainty. According to the IMF's latest World Economic Outlook Update (January 2024), global GDP growth is estimated to decelerate marginally from 3.4% in FY22 to 3.1% in FY23, followed by a slight recovery, expected to reach 3.2% by FY2024. Various challenges persist, impacting economic activity worldwide. Globally, Central banks have significantly raised interest rates to counter inflation, leading to tightened financial conditions. Geopolitical tensions, such as the Russia-Ukraine war, have exacerbated supply chain disruptions, energy and food crises, and security concerns on a global scale. Lockdowns in China to manage new Covid-19 outbreaks have affected manufacturing and trade flows, leading to inflation. As a result, increasing living costs, segmented labor markets, weaker fiscal support, and elevated debt levels constrain consumer purchasing power and confidence, with limited government space for stimulus measures.



PAKISTAN

In FY23, Pakistan's economy faced a multitude of challenges. The war in Ukraine led to supply disruptions, while the country was still grappling with the aftermath of the previous year's floods. Political uncertainties further compounded these issues, along with inflation, currency depreciation, and dwindling forex reserves. In response, the State Bank of Pakistan raised interest rates, and the government implemented import restrictions, increased energy prices, and raised corporate taxes. However, these fiscal and monetary measures resulted in supply chain disruptions, contributing to a GDP contraction to 0.29% in FY23 compared to 5.7% growth in FY22.

Looking ahead, the World Bank has projected a recovery in Pakistan's real GDP growth, reaching 1.7% in FY24; despite the country facing one of its worst crises due to poor policy choices combined with a series of shocks. The International Monetary Fund (IMF) also expects Pakistan to achieve a modest economic growth rate of 2.5 percent in FY24.

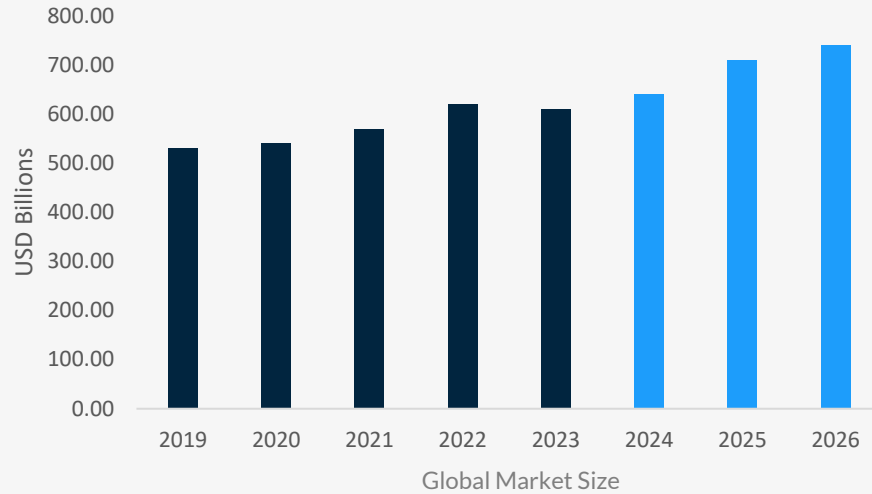
The World Bank suggests that Pakistan must address its human capital crisis and generate more fiscal space to finance improvements in service delivery and human capital development. However, political turmoil is expected to slow down growth in private demand. If inflationary pressure eases, growth is expected to pick up to 2.4% in FY25. These challenges call for deep, sustained reforms. The alternative of muddling through with short-term fixes and external financing is riskier and much harder to pull off.

HOUSEHOLD APPLIANCES INDUSTRY

GLOBAL

The global household appliances market expanded from USD 551.29 billion in 2022 to USD 606.58 billion in 2023. The Russia-Ukraine conflict disrupted the global economic rebound from the COVID-19 pandemic, resulting in economic sanctions, commodity price hikes, and supply chain interruptions; therefore, leading to inflation across various sectors. The household appliances market is forecasted to reach USD 859.71 billion by 2027, with a compound annual growth rate (CAGR) of 9.1%. Technological advancements, particularly in smart appliances, are expected to fuel market growth. Smart appliances, known for advanced features and energy efficiency, appeal to consumers seeking convenience and enhanced functionalities. Wireless technologies such as Wi-Fi and Bluetooth are increasingly integrated into appliances, catering to tech-savvy consumers. The market presents growth prospects through affordability, product innovation, and increasing replacement sales in developed regions due to rising per capita income and urbanization.

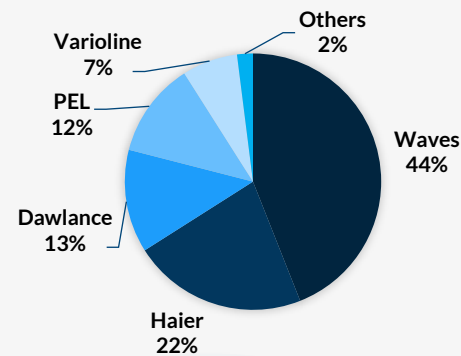
Asia-Pacific dominates the global household appliance market revenue share (~40%). Developed nations like Japan, Singapore, Hong Kong, and Indonesia anticipate higher sales of smart appliances driven by factors like rising energy and labor costs, strong consumer purchasing power, and increased awareness of smart city initiatives. China stands out with the highest demand for traditional air conditioners globally, supported by energy-efficient appliance policies, a thriving property market, and warm weather.



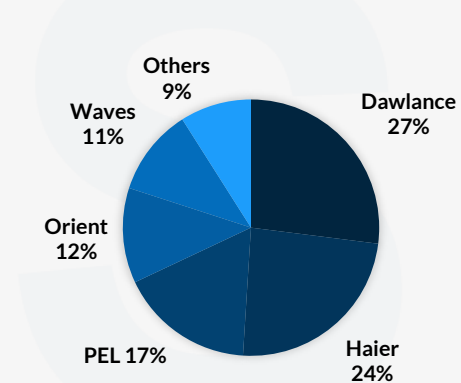
PAKISTAN

The Household Appliance Sector of Pakistan is a sub-segment of the 'Electrical Equipment' group within the large-scale manufacturing sector. It accounts for ~2% of the Large-Scale Manufacturing (LSM) sub-segment of the economy. As it is a 'brand' driven market, pricing and marketing strategies play a key role in attracting market shares and can vary entirely for different players among different product segments. In addition, as an industry dominated by well recognized brands, extensive capital requirement and long cash cycle act as high entry barriers. Duty protection in the form of additional customs and regulatory duties provides price advantage to local players.

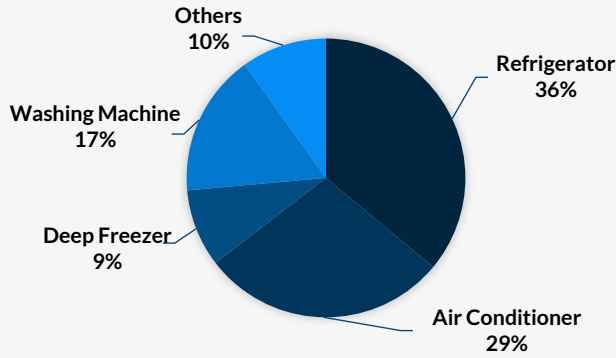
The Household Appliances market generates demand from both original (first-hand) and replacement markets. Growth is directly related to per capita income, population growth, technological innovation, energy-efficient products, rapid urbanization, and seasonality. In terms of major products, refrigerators have the highest value share, followed by air conditioners, televisions, washing machines, deep freezers, and other products.



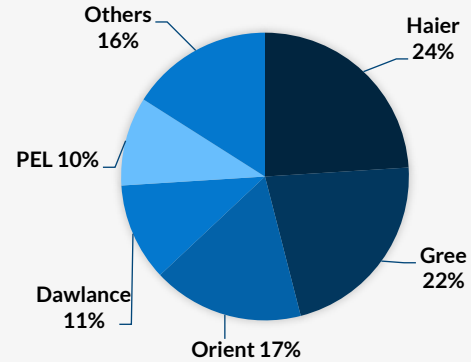
Deep Freezer Market Shares (%)



Refrigerator Market Shares (%)

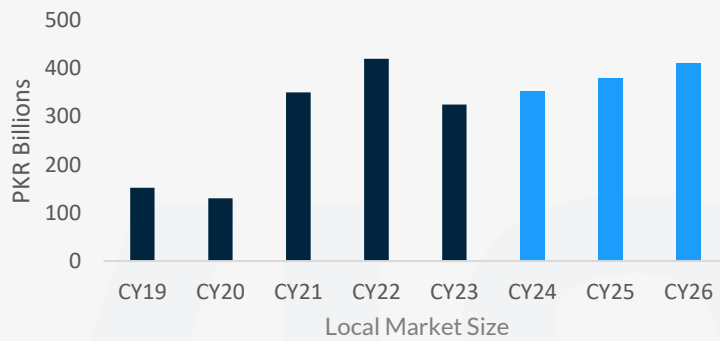


Revenue Based Market Composition (%)

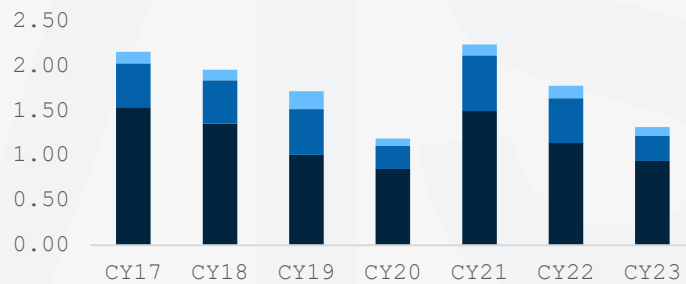


Air Conditioner Market Shares (%)

During CY23, the industry was marred by the slump in demand in the wake of stressed economic activity and an erosion in consumer disposable income. Furthermore, production constraints resulting from import restrictions exacerbated the sector's performance challenges. As such the market size in CY23 reported severe contraction. Although some improvements have been observed in macroeconomic conditions, persistent issues such as high energy costs, inflation, and interest rates continue to pose obstacles to the industry's growth prospects going forward. The estimated size of the industry in CY23, in dollar terms has declined to ~USD 1.2 bln (CY22: ~USD 2.1 bln) or PKR 325 bln (CY22: PKR 420 bln). Loss in dollar terms was greater than in rupee terms on account of significant depreciation of the local currency between CY22-CY23.



Local Market Size



■ Refrigerators ■ Airconditioners ■ Deepfreezers

Production Volumes of Major Appliances in Millions

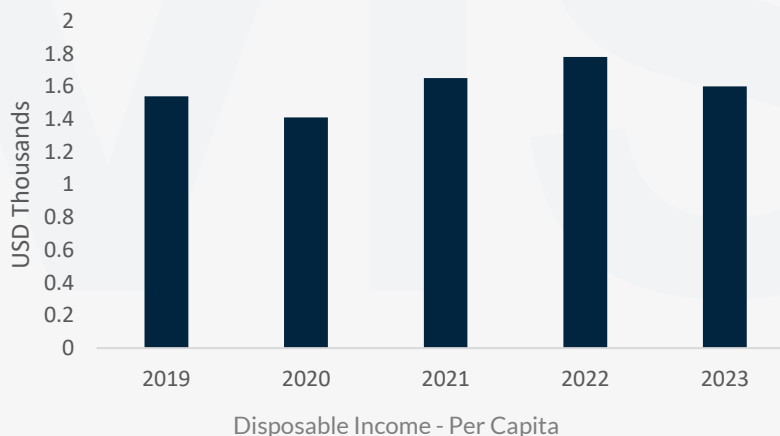
SECTOR DRIVERS

- Population growth:** Pakistan has a large population, approximately 3% of the world’s population. As per the 2023 census conducted by Pakistan Bureau of Statistics, the country has a total population 241.5 million people, reporting a growth of 13.3% over the previous official numbers. Growth in population is also directly correlated with consumer household products and provides a base demand to the sector.
- Urbanization:** Urbanization is also a major proponent of demand in the household appliances sector, as it indicates improvement in living standards and move of consumers to modern products. Since, 2018 Pakistan has reported an average urbanization rate of 2.4%, with a continuous growth trend over the last 5 years.
- Tariff Protection:** Local producers retain a substantial portion of the market share in key segments, aided by duty protection measures such as additional custom and regulatory duties, which afford local players a pricing advant

Duty Structure	Regulatory Duty	Custom Duty	Additional Custom Duty
Stoves, ranges, grates, cookers (including those with subsidiary boilers for central heating), barbecues, braziers, gas- rings, plate warmers and similar non- electric domestic appliances, and parts thereof, of iron or steel. (includes CKD/SKD units)	10-15%	20%	6%
Air conditioning machines, comprising a motor driven fan and elements for changing the temperature and humidity, including those machines in which the humidity cannot be separately regulated. (Includes CKD/SKD units)	5%	20%	6%
Refrigerators, freezers and other refrigerating or freezing equipment, electric or other; (Includes CKD/SKD units)	20%	20%	6%

SECTOR CONSTRAINTS

- Erosion in Disposable Income:** While usually a demand driver, a contraction of disposable income as reported in 2023 can also be a constraint on the sector’s performance. Disposable income per capita declined from ~USD 1,780



in 2022 to ~USD 1,600 in 2023. This was mostly on account of a significant erosion in the value of the local currency against the dollar, coupled with resultant inflation and other economic challenges.

- High Import Dependence:** The local household appliances industry is mainly involved in assembling finished products. Major cost component – Complete Knockdown (CKD) kits are imported, generally from China. With depreciation of the rupee (PKR), the cost of CKD kits surged, leading to exponential increase in prices of the end products, which also adversely impacted volumetric sales.
- Competition:** Competition within the sector is characterized as medium to high, with participation from both local and international entities. As a result, pricing power is constrained for sector participants, posing challenges to margin maintenance during periods of high currency volatility and inflation.

SECTOR OUTLOOK

OVERALL ASSESSMENT/OUTLOOK: STABLE

While CY23 was a difficult year for the sector, some improvements have been observed in macroeconomic conditions during the ongoing CY24. Volume stabilization is anticipated after reaching a low point, with topline growth expected to be supported by price adjustments from sector participants. Additionally, duty protection against imported products contributes to a 'Stable' outlook for local players in the Household Appliances industry. However, ongoing challenges such as high energy costs, inflation, and interest rates persist, presenting obstacles to the industry's future growth prospects.

VIS RATING UNIVERSE

HOUSEHOLD APPLIANCES COVERAGE

VIS has three ratings outstanding from the household appliances sector of Pakistan, rated within the A (Single-A) band with short-term ratings of A-2 (A-Two).

Summary of VIS Household appliances Ratings Universe			
Company	Long-term Rating	Short-term Rating	Outlook
Waves Household appliances Limited	A	A-2	Stable
Digital World Pakistan (Pvt.) Limited	A-	A-2	Negative
Orient Electronics (Pvt) Limited	A-	A-2	Rating Watch - Negative

Rating scale and Definitions may be accessed at (<https://docs.vis.com.pk/docs/VISRatingScales.pdf>)

KEY SECTORAL METRICS

Metrics	Sector Average				Sector Median			
	2020	2021	2022	2023	2020	2021	2022	2023
Gross Margin (%)	20.08%	20.03%	20.62%	24.09%	20.08%	20.01%	19.60%	24.60%
Net Profit Margin (%)	4.25%	3.17%	2.80%	2.02%	4.25%	3.49%	3.34%	2.72%
FFO to Total Debt (x)	0.14	0.07	0.12	0.04	0.14	0.08	0.09	0.04
FFO to Long Term Debt (x)	0.67	0.50	1.09	0.12	0.67	0.22	0.46	0.10
Leverage (x)	2.22	2.29	2.35	1.58	2.22	1.67	1.98	1.47
Gearing (x)	1.08	1.03	1.17	0.84	1.08	1.02	1.00	0.88
DSCR (x)	1.77	1.24	1.43	0.82	1.77	1.16	0.90	0.84
Current Ratio (x)	1.16	1.28	1.16	1.17	1.16	1.14	1.16	1.20

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- Pakistan Bureau of Statistics
- Pakistan Electronics Manufacturers' Association
- International Monetary Funds
- World Bank Database
- Statista
- VIS Database
- Global data

RESEARCH & PUBLICATIONS

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Jahangir Kothari Parade (Lady Lloyd Pier) Inspired by Her Excellency, The Honorable Lady Lloyd, this promenade pier and pavillion was constructed at a cost of 3 Lakhs and donated to the public of Karachi by Jahangir Kothari to whose generosity and public spirit the gift is due. Foundation stone laid on January 5, 1920. Opened by Her Excellency, The Honorable Lady Lloyd on March 21, 1921.

Dome: A roof or vault, usually hemispherical in form. Until the 19th century, domes were constructed of masonry, of wood, or of combinations of the two, frequently reinforced with iron chains around the base to counteract the outward thrust of the structure.

Origins: The dome seems to have developed as roofing for circular mud-brick huts in ancient Mesopotamia about 6000 years ago. In the 14th century B.C. the Mycenaean Greeks built tombs roofed with steep corbeled domes in the shape of pointed beehives (tholos tombs). Otherwise, the dome was not important in ancient Greek architecture. The Romans developed the masonry dome in its purest form, culminating in a temple built by the emperor Hadrian. Set on a massive circular drum the coffered dome forms a perfect hemisphere on the interior, with a large oculus (eye) in its center to admit light.

VIS Credit Rating Company Limited is committed to the protection of investors and offers a blend of local expertise and international experience to serve the domestic financial markets. With its international reach, VIS is positioned to aim for an international mark. In this regard, the global experience of our international affiliates and partners have been invaluable towards adding depth to our ongoing research endeavors, enriching us in ways, that enable us to deliver our responsibilities to the satisfaction of all investors. The edifice of the Jahangir Kothari Parade has stood proudly through the years and is a symbol of our heritage. Its 'Dome' as the most stable of building structures, exemplifies architectural perfection. Committed to excellence, VIS continues its endeavour to remain an emblem of trust.

INTERNATIONAL

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Collaborations

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China Chengxin International Credit Rating Company Limited - China

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