

RATING REPORT

Inbox Business Technologies Limited

REPORT DATE:

March 18, 2020

RATING ANALYSTS:

Narendar Shankar Lal

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RATING DETAILS		
Rating Category	Initial Rating	
	Long-term	Short-term
Entity	BBB-	A-3
Rating Outlook	Stable	
Rating Date	March 18, 2020	
Rating Action	Initial	

COMPANY INFORMATION

Incorporated in 2001	External auditors: EY Ford Rhodes Chartered Accountants, Karachi
Public Unlisted Company	Chief Executive Officer: Mr. Mohsin Ali
Key Shareholders (with stake 5% or more):	
Patek (Private) Limited – 99.99%	

APPLICABLE METHODOLOGY (IES)

VIS Entity Rating Criteria *Industrial Corporates (April 2019)*

<https://s3-us-west-2.amazonaws.com/backupsqvis/docs/Corporate-Methodology-201904.pdf>

Inbox Business Technologies Limited

OVERVIEW OF THE INSTITUTION

Incorporated in 2001, Inbox Business Technologies operates as a public unlisted company. Registered office of the company is based in Karachi.

Profile of CEO

Mr. Mohsin Ali is a seasoned professional with over 17 years of experience in Information Technology (IT). He has served in leading local and multinational organizations. He holds BBA (Hons) in Finance Degree from Foundation University.

RATING RATIONALE

Inbox Business Technologies Limited (IBTL) is engaged in the business of manufacturing, selling of IT equipment, Managed IT services and provision of network and security system solutions. The company classifies its business operations into three segments: Enterprise Management Services (EMS), Citizen Services (CSX) and Digital Security and Infrastructure (DSI). Managed services segment includes revenue generated from provision of end-to-end IT infrastructure management services to private clients. Citizen Services segment includes all the public sector projects. Digital Security and Infrastructure segment includes revenue generated from various transaction businesses catering to the telecom industry and the Financial Sector.

Key Rating Drivers

Sound Sponsor Profile

IBTL is a wholly owned subsidiary of Patek (Pvt.) Limited, which is a private investment holding company with shareholding vested with family members of Dawood Group. The assigned ratings incorporate demonstrated support from the sponsor as evident in form of equity injection as advance against future issuance of shares in 2018 which has been converted into equity during Q4'2019.

Business risk profile is supported by sizeable quantum of medium to long tenor contracts in hand, healthy contract renewal rate for public and private sector projects, adequate barriers to entry and modest competition. Client wise concentration in revenues, delay in payments from government projects, changes in the discount rate and exposure to exchange rate fluctuations are considered key risk factors

EMS and CSX segment contracts have an average tenor of 3 years, while the company has also experienced a healthy renewal rate of 80% in both these segments historically. Presently, one major contract in DSI segment also has a tenor of 3 years, while the remaining contracts are renewed on yearly basis. Considering sizeable medium to long tenor of contracts and healthy renewal rate in two segments, revenue visibility is considered to be on the higher side over the ratings horizon. Operational history of the company to add new business to its portfolio on yearly basis also provides comfort to the ratings.

EMS and CSX segments are also characterized by significant barriers to entry as specialized resources and significant geographical footprint is required across the country to cater to the requirements of large clients. Both these factors provide a competitive edge to IBTL. The company is exposed to significant competition in the DSI segment due to presence of many competitors.

Client wise concentration in revenues is considered to be on the higher side with top 10 clients comprising 98.8% (2018: 84.8%; 2017: 95.3%) of total revenues in 9M'2019. Long term association and committed business with many large clients partly mitigates the client concentration risk. As public sector projects account for majority revenues of the company, IBTL is also susceptible to delay in payments by the government. However, management at IBTL is working to restructure majority of its customer base from government to private clients to reduce the reliance on the government sector.

A certain proportion of IBTL purchases are denominated in US dollars, which exposes the company to volatility in exchange rates. However, net impact of rupee devaluation on company's financial profile is considered limited as a portion of company's revenues are also denominated in US dollars.

Profitability has witnessed improvement on timeline basis due to reduction in overheads

Topline of the company witnessed significant reduction post 2016 due to completion of few large one-off projects. Post 2016, the management has mostly focused on recurring annuity business which has enabled the company to sustain the revenues in 2017 and 2018. However, sizeable growth in topline is projected during the full year 2019 due to induction of new projects coupled with growth in revenues from existing clients. Growth momentum in revenues is expected to persist over the ratings horizon.

Gross margins have depicted an improving trend in the period from 2016 to 2018. Overall profitability of the company has varied in line with topline of the company. With reduction in topline post 2016 and expenses base mainly comprising fixed overheads, the company posted net loss in 2017 and 2018. However, improvement has been witnessed in profitability profile as the quantum of loss has depicted reduction on timeline basis. IBTL is expected to post net profit in coming years. Improvement in profitability is primarily attributed to reduction in salary and wages expenses through right sizing of headcount. As per management, implementation of variable pay model is expected to help further in optimizing costs, going forward. Focus on maintaining headcount at adequate level will remain a priority of the management. With projected growth in topline and continuation of cost cutting measures, profitability is expected to depict an increasing trend, going forward.

Liquidity profile is considered adequate

Funds flow from operations (FFO) has varied in line profitability of the company. FFO in relation to total debt amounted to 2% (2018: 12%; 2017: -3%; 2016: 14%) in 9M'2019. The company's cash conversion cycle is considered stretched. However, improvement has been witnessed during the ongoing year as the management has prioritized recovery of receivables from clients. Along with improvement in cash conversion cycle, lower projected outflow for capital expenditure in relation to internally generated cash flows is expected to provide support to the liquidity profile, going forward.

Leveraged capital structure

Equity base has increased on timeline basis due to injection of additional capital and improvement in profitability profile of the company; however, quantum of total debt has remained at approximately similar level. In view of this scenario, leverage indicators are reported lower vis-à-vis 2016. Gearing and Leverage ratios of the company were reported at 3.0x (2018: 2.4x; 2017: 5.5x; 2016: 3.6x) and 3.7x (2018: 3.0x; 2017: 6.4x; 2016: 5.0x), respectively at end-9M'2019. Management plans to reduce the reliance on borrowings going forward, which is expected to translate to improvement in leverage indicators. Improvement in leverage indicators in line with projections is considered important from ratings perspective.

Corporate governance framework is satisfactory

The Board of Directors (BoD) at IBTL comprises seven Non-Executive Directors. In line with best practices, a female director is also present on the Board. Management may consider appointment of independent directors to further align Board composition with the best practices. In order to ensure effective oversight, Board Audit Committee (BAC) and Board Human Resource and Remuneration Committee (BHRRC) are also present. Scope of internal audit function is considered comprehensive as the department covers all the back and front office functions along with special assignments advised by the CEO or BAC. The Chief Internal Auditor (CIA) reports functionally to the Chairman of IBTL's Board Audit Committee (BAC) and administratively to the Chief Executive Officer (CEO) of IBTL.

Inbox Business Technologies Limited
Appendix I

FINANCIAL SUMMARY				
	<i>(amounts in PKR millions)</i>			
<u>BALANCE SHEET</u>	2016	2017	2018	9M'19
Property and Equipment	1,040.0	929.9	1,059.6	1,185.0
Total Fixed Assets	1,097.8	1,053.9	1,213.5	1,424.8
Stock-in-Trade	163.5	241.7	637.6	718.5
Trade Debts	2,717.7	1,886.7	1,791.2	998.9
Cash & Bank Balances	195.7	150.9	119.0	671.5
Total Assets	5,251.9	4,125.9	4,918.0	4,947.3
Adjusted Trade and Other Payables	1,113.8	463.7	536.2	586.9
Adjusted Total Debt	3,174.7	3,042.8	3,019.0	3,097.4
Paid up capital	71.0	710.1	710.1	710.1
Advance against issue of shares	-	-	718.0	718.0
Total Equity (excluding revaluation surplus)	876.9	555.7	1,241.9	1,042.8
<u>INCOME STATEMENT</u>				
Net Sales	4,445.4	2,490.7	2,482.4	2,053.8
Gross Profit	1,271.7	639.4	853.4	444.7
Profit Before Tax	374.6	(292.3)	27.8	(206.8)
Profit After Tax	266.9	(321.2)	(31.8)	(199.1)
<u>RATIO ANALYSIS</u>				
Gross Margin (%)	28.6%	25.7%	34.4%	21.7%
Trade debts/Sales	61.1%	75.8%	72.2%	48.6%
FFO	437.4	(94.5)	363.6	40.5
FFO to Total Debt (%)	13.8%	-3.1%	12.0%	1.7%
FFO to Long Term Debt (%)	113.6%	-28.7%	115.2%	11.3%
Current Ratio (x)	1.0	0.9	1.0	0.9
Gearing (x)	3.6	5.5	2.4	3.0
Leverage (x)	5.0	6.4	3.0	3.7

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	Inbox Business Technologies Limited				
Sector	Information Technology				
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				
	18/03/2020	BBB-	A-3	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.				
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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Due Diligence Meetings Conducted		Name	Designation	Date	
	1	Mr. Shakeel Farooq	Acting CFO	December 19, 2019	
	2	Ms. Samina Malik	Chief Human Capital Officer	December 19, 2019	