Ncell Axiata Limited: Ratings reaffirmed

September 27, 2023

Summary of rating action:

Instrument* (Amounts in NPR Million)	Previous rated amount	Current rated amount	Rating Action
Long-term loans	18,645	15,225	**[ICRANP] LA**; reaffirmed
Short-term loans	10,000	12,000	**[ICRANP] A1**; reaffirmed
Total	**28,645**	**27,225**	

** Instrument details are provided in Annexure-1*

Rating action

ICRA Nepal has reaffirmed the long-term rating of **[ICRANP] LA** (pronounced ICRA NP L A) assigned to the long-term loans of Ncell Axiata Limited (Ncell or the company). ICRA Nepal also reaffirmed the short-term rating of **[ICRANP] A1** (pronounced ICRA NP A one) to the enhanced short-term loan limits of Ncell.

Rationale

The ratings reaffirmation continues to factor in the company's strong financial profile with gearing of 0.9 times and total debt (TD) to OPBDITA of 0.8 times as of mid-July 2023. Despite the decline in revenues in line with the industry trends, the company's profitability indicators continue to remain robust with operating profit margins (OPM) of ~53% in FY2023. Given its comfortable leverage levels and largely steady margins, Ncell continued to report a healthy DSCR of ~3.2 times in FY2023, notwithstanding the decline in recent years on account of spiked interest rates. With lowering term loan burden, incremental debt servicing indicators are expected to remain comfortable, despite expected slight moderations in OPM going forward. The ratings also continue to factor in the company's strong promoter profile with ~80% stake ultimately held by the Axiata Group Berhad[1], which has a good track record in the telecommunication sector across multiple Asian countries. Accordingly, experienced board members and seasoned management team continue to remain the rating positives for the company. Ncell's comfortable liquidity profile with sizeable unutilised drawing power and the extended credit support from capex creditors also support the rating action. ICRA Nepal also takes positive note of the company's long track record of operations (since 2005, as the first private sector GSM operator in the country), high entry barriers for new entrants and a saturated user base when compared with Nepal's demographics.

Nonetheless, the ratings remain constrained by the sustained decline in the company's revenue market share to ~54% in FY2022[2] (~61% in FY2020) along with the competition induced decline in average revenue per user (ARPU) metrics. ICRA Nepal also takes note of the major spike in the company's contingent liabilities (~NPR 65 billion as of mid-July 2022, ~89% of which were tax claims relating to the ownership change in the past). The company also continues to maintain high commitment towards shareholders' returns as reflected by steadily high dividend pay-out trends. In line with the past trends, Ncell reported a weak current ratio at 0.65 times along with modest total outsider liabilities to tangible net worth ratio at 3.2 times as of mid-July 2023, owing to the sizeable capex related payables. High regulatory and technological obsolescence risks for the telecom industry, in addition to the sizeable regular as well as technological advancement related capex requirements also remains a rating concern. Going forward, any key developments regarding the contingent liabilities would remain a major rating monitorable. Ncell's ability to maintain/improve its operational and financial profile in terms of market share, revenues/profitability and hence its ability to maintain comfortable capitalisation and coverage indicators, will remain the key rating sensitivities.

[1] Rated by Moody's at Baa2.

2 Market share data for FY2023 not exactly ascertainable in lack of segmental revenues of the company's competitors.

Key rating drivers

Credit strengths

Robust capitalisation and coverage indicators – Ncell has been maintaining sizeable reserves, despite the trend of high dividend pay-outs. Hence, the company's capitalisation and coverage indicators continue to remain robust, with gearing of 0.9 times and TD/OPBIDTA of 0.8 times as on mid-July 2023. With a sizeable cash balance, the company's net debt to OPBITDA ratio remained comfortable at 0.2 times as of mid-July 2023. The indicators are expected to further improve with the lowering term debt burden.

Largely steady profitability and comfortable liquidity profile – Despite the gradual decline over the years, the company's OPM still remain healthy at ~53% for FY2023. While the shrinking revenues from voice and international long distance (ILD) revenues have impacted margins to an extent, the company's cost control strategies have restricted higher correction in margins. Despite the general industry wide trend of declining overall APRU (including voice and data revenues), Ncell still continues to command ~50% market share in voice revenues; and even a higher market share in the data segment at ~57% for FY2022. Recent gradual increase in the data ARPU and increasing data usage per user could remain a positive for future revenues/margins, both of which are likely to be increasingly reliant on data. Comparatively higher ARPU along with other entry barriers to the industry also continue to remain a rating positive. The company's liquidity profile also remains comfortable with sizeable cushion in terms of unutilised drawing power (~65% as of mid-July 2023). The elongated credit period for capex costs by virtue of its group strengths, also supports its liquidity profile.

Strong promoter profile and experienced directors/management – The company is a part of the Axiata Group Berhad (Axiata), following an indirect acquisition of ~80% stake in the company in April 2016 (rest ~20% being held by local partner viz. Sunivera Capital Venture Private Limited). Axiata, the major promoter group, has an extensive experience in telecom sector spanning multiple countries in Asia and is one of largest regional cellular telecommunication service providers in Asia. The ensuing augmentation of experienced directors and the management team remains a positive for the company's business performance going forward.

Credit challenges

Declining market share – The company has been reporting steady decline in GSM revenue market share which stood at ~54% in FY2022 from ~61% in FY2020. While the company's market share in terms of subscriber base remains even lower at ~42% as of mid-July 2022, relatively better APRU has aided it in maintaining ~54% market share in terms of overall GSM revenues. While the voice ARPU has largely followed the industry trend of general decline, data ARPU has shown slight improvement in recent years, which remains a positive. However, the public sector competitor i.e. Nepal Telecom has been achieving relatively higher 4G penetration in recent years, thus remaining a rating concern.

Large contingent liabilities and high commitment to shareholder returns – Ncell has reported a major spike in contingent liabilities (~NPR 65 billion as of mid-July 2022 from ~NPR 5 billion a year ago), ~89% of which related to the tax related claims for the past changes in ownership, after having already paid ~NPR 47 billion in capital gains taxes (including fixes and penalties) relating to the same event. Hence, any major materialization of the same would have a significant impact on the company's financial profile and therefore remains a key rating monitorable. The company's dividend payout has also generally remained high (an average of ~94% in the last three years; dividends paid out during FY2023 were ~90% of FY2022 profits). Any sizeable increment in dividend payout impacting the company's reserves would have a bearing over the company's financial metrices and hence might have a bearing over the assigned ratings.

High capex payables leading to weak current ratio – The company has sizeable capex related payables in its books at ~NPR 14 billion as of mid-July 2023, pressurizing its current ratio, which stood at 0.65 times as on the same date. Though the implementation timelines and payment terms for these are quite elongated, any uneven payment timelines of the same could pressurize the interim liquidity.

Risk of regulatory changes and technological obsolescence – Telecom industry in general is susceptible to any significant changes in Government policies which could have a bearing on the performance of the company. Further, the company needs to ensure sizeable amounts of regular capex to upgrade its services/quality. These investments are also subject to technological risks arising from advancements in the field of telecommunications technology.

Link to the last rating rationale:
Ncell-Axiata-Limited-BLR Surveillance_August 2022

Analytical approach: For arriving at the ratings, ICRA Nepal has applied its rating methodology as indicated below.

Links to applicable criteria
Corporate Credit Rating Methodology

About the company

Incorporated in 2001 as Spice Nepal Private Limited, the company started its commercial operations from September 2005, as the first private sector GSM telecom operator of Nepal, under the brand name "Mero Mobile". Later in September 2008, European telecom giant Teliasonera acquired controlling stake in the company and the brand name was changed to "Ncell" in March 2010, followed by the change in company's name to Ncell Private Limited. On April 12, 2016, the company became a part of the Axiata Group Berhad, when the Group bought 100% shares of Reynolds Holding Limited of West Indies, which holds 80% stake in the company (rest 20% stake is held by Sunivera Capital Venture Private Limited of Nepal). Following this, the company's name was again changed to Ncell Axiata Limited (Ncell) and it was converted to public limited company on August 03, 2020.

Key financial indicators

	FY2020 (Audited)	FY2021 (Audited)	FY2022 (Audited)	FY2023 (Provisional)
Operating income (OI; NPR million)	46,874	40,424	39,725	37,442
OPBITDA/OI (%)	54%	56%	55%	53%
Total debt/Tangible net worth (TNW; times)	1.0	1.2	1.1	0.9
Total outside liabilities/TNW (times)	4.9	3.3	3.4	3.2
Total debt/OPBITDA (times)	0.8	1.0	1.0	0.8
Interest coverage (times)	18.1	9.0	9.0	8.1
DSCR (times)	14.3	4.6	3.7	3.2
Net working capital/OI (%)	-49%	-44%	-45%	-36%
Current ratio	0.59	0.56	0.68	0.65

Source: Company data

Annexure-1: Instrument details

Instrument (Amounts in NPR Million)	Last rated amount	Current rated amount	Rating Action
Long term limits (A)	**18,645**	**15,225**	**[ICRANP] LA**; reaffirmed
Fund-based limits; Term loan	18,645	15,225	
Short term limits (B)	**10,000**	**12,000**	**[ICRANP] A1**; reaffirmed
Fund-based limits; Working capital loan	4,000	4,000	
Non-fund-based limits; Letter of credit	6,000	8,000	
Total (A+B)	**28,645**	**27,225**	

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About ICRA Nepal Limited

ICRA Nepal Limited, the first credit rating agency of Nepal, is a subsidiary of ICRA Limited (ICRA) of India. It was licenced by the Securities Board of Nepal (SEBON) on October 3, 2012. ICRA Nepal is supported by ICRA Limited through a technical support services agreement, which envisages ICRA helping ICRA Nepal in areas such as rating process and methodologies, analytical software, research, training, and technical and analytical skill augmentation.

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