

## Air Link Communications Limited

Transitioning into a vertically integrated mobile player

Thursday, August 26, 2021

Air Link Communication Limited intends to offer 90Mn shares (25% of its post paid up share capital) to the general public, in the form of 60Mn new shares and 30Mn offer-for-sale by the largest sponsor of the company, Mr. Muzaffar Hayat Piracha. At its floor price, the company intends to raise PKR 5.8Bn, making it the largest IPO in the history of Pakistan. The company has shown exceptional 5-year revenue and PAT CAGR of 49% and 29%, respectively. It is worth highlighting that the company started off from a small revenue base of PKR 140Mn in FY10 and has grown impressively to PKR 47Bn revenues in a period of just 11 years. Going forward, the company is expected to undergo a 5-year revenue CAGR of 26%, which is considerable given the high base of FY21. We recommend subscribing up to the ceiling price of PKR 91/sh, which translates into FY22E P/E of 8.9x. The company has no direct match on the bourse, therefore, we have applied a 45% discount to the weighted average industry P/E of 26.2x to arrive at target P/E multiple of 11.8x and FV of PKR 120/sh for Air Link.

**First company to introduce 3G enabled smart phones:** Air Link Communication (Pvt.) Limited, founded in Aug'2010, is a leading distributor of mobile phones with a strong presence in Pakistan with service centers across the country. The company registered itself as an Association of Persons ("AOP") when it introduced Pakistan's first 3G-enabled (GSM + EVDO) Android smartphone and first 3G-enabled dual mode (GSM + EVDO) Android tablet in partnership with PTCL. Air Link Communication (Pvt.) Limited was incorporated on Jan'14 to take over the existing business of the AOP by acquiring all assets and liabilities. With effect from Apr'19, the company was converted into an unlisted public limited company.

**A leading distributor of mobile phones:** The company is a leading distributor of mobile phones in Pakistan engaged in both import and distribution of Huawei and Samsung mobile phones & accessories. The market share currently stands between 20-25% as per Customs Import Data. It is the official partner of Samsung mobiles and tablets in the territory of Pakistan & Afghanistan with the country-wide distribution network comprising of 16 regional hubs linked to 1,000+ wholesalers and 4,000+ retailers for ultimate selling of mobile phones and accessories. The company has become a completely integrated mobile phone player after establishing a handset assembly unit in Lahore with a production capacity of 400,000 units per month. Air Link is assembling low cost mobile phones (TCL, ITel and Tecno) at this facility.

Table 1: IPO Details

IPO strike price - floor (PKR/sh.)	65
IPO strike price - ceiling (PKR/sh.)	91
IPO Stock offer (Mn)	90
Pre - IPO Shares (Mn)	300
Post - IPO shares (Mn)	360
M.Cap at floor (PKR Mn)	23,400
M.Cap at floor (USD Mn)	143
M.Cap at ceiling (PKR Mn)	32,760
M.Cap at ceiling (USD Mn)	200

Source: Air Link Prospectus

Table 2: Shareholding pattern

Share (Mn)	Pre IPO	Post IPO
Muzaffar Hayat Piracha	121.80	91.80
Other sponsors	178.20	178.20
Other Directors	0.00	0.00
General public (IPO)	0.00	90.00
<b>Total (Mn)</b>	<b>300</b>	<b>360</b>

Source: Air Link Prospectus

Table 3: Source and utilization of funds

	PKR Mn
<b>Source</b>	
New Issue Proceeds	3,900
Short Term Financing	990
<b>Total</b>	<b>4,890</b>
<b>Utilization</b>	
Working Capital	4,890

Source: Air Link Prospectus

Table 4: Air Link Communications—Financial Snapshot

	FY19	FY20	FY21E	FY22F	FY23F
EPS - Pre IPO	4.93	4.88	4.95	12.23	17.96
EPS - Post IPO	4.11	4.07	4.12	10.19	14.42
P/E (x)	15.81	15.98	15.76	6.38	4.34
ROE (%)	47.12	31.85	24.86	28.09	33.08
D/E (x)	2.50	1.96	0.79	0.15	0.12
Sales Growth (%)	23.33	44.39	11.16	48.82	20.20
Gross Margins (%)	13.38	11.09	9.32	12.06	13.50
PAT Growth (%)	19.94	(1.06)	1.40	147.03	46.95

Source: Air Link Prospectus, BMA Research

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**BMA Capital Management Ltd.**

## Air Link: Summary of Financials

**Table 5: Income Statement**

PKR Mn	FY19	FY20	FY21E	FY22F	FY23F
Sales	29,786	43,008	47,806	71,148	85,517
Cost of Sales	25,799	38,238	43,351	62,566	73,975
<b>Gross Profit</b>	<b>3,989</b>	<b>4,770</b>	<b>4,456</b>	<b>8,582</b>	<b>11,541</b>
Distribution cost	307	519	483	1,131	1,127
Administrative/ Conversion Expense	433	477	705	1,942	2,598
<b>Operating profit</b>	<b>3,246</b>	<b>3,774</b>	<b>3,269</b>	<b>5,509</b>	<b>7,816</b>
Other income	176	168	92	69	84
Finance cost	827	1,398	1,031	412	310
<b>Profit before taxation</b>	<b>2,595</b>	<b>2,544</b>	<b>2,329</b>	<b>5,166</b>	<b>7,591</b>
Taxation	1,115	1,080	845	1,498	2,201
<b>Profit after taxation</b>	<b>1,480</b>	<b>1,464</b>	<b>1,485</b>	<b>3,668</b>	<b>5,389</b>
Pre-IPO EPS	4.93	4.88	4.95	12.23	17.96
Post-IPO & debt conversion EPS	4.11	4.07	4.12	10.19	14.42
DPS	0.00	0.00	0.00	3.50	6.00

Source: Company Projections, BMA Research

**Table 6: Balance Sheet**

PKR Mn	FY19	FY20	FY21E	FY22F	FY23F
Property & equipment	109	477	924	1,161	2,858
Intangible assets	4	9	4	36	41
Deferred tax asset	210	81	-	-	-
<b>Non-current assets</b>	<b>323</b>	<b>567</b>	<b>928</b>	<b>1,197</b>	<b>2,899</b>
Stock in trade	1,118	4,610	4,032	6,857	7,094
Short term investments	2,508	726	821	1,021	1,221
Trade debts	5,125	4,655	4,578	3,895	4,682
Advances, deposits and prepayments	5,612	9,602	2,030	1,249	1,424
Cash and bank balances	282	814	964	1,998	2,202
<b>Current assets</b>	<b>14,645</b>	<b>20,408</b>	<b>12,425</b>	<b>15,020</b>	<b>16,621</b>
<b>Total assets</b>	<b>14,968</b>	<b>20,975</b>	<b>13,353</b>	<b>16,217</b>	<b>19,520</b>
Paid up capital	2,617	3,109	3,000	7,700	7,700
Retained earnings	524	1,488	2,972	5,356	8,590
<b>Total equity</b>	<b>3,141</b>	<b>4,597</b>	<b>5,972</b>	<b>13,056</b>	<b>16,290</b>
Finance lease obligation	22	295	17	9	5
Long term loan	757	413	429	-	-
Net defined benefit liability	23	29	32	35	39
<b>Non-current liabilities</b>	<b>803</b>	<b>737</b>	<b>477</b>	<b>44</b>	<b>44</b>
Short term bank borrowing	7,082	8,184	3,872	2,004	1,927
Current portion of liabilities against finance lease	11	75	10	13	8
Provision for taxation	219	197	-	-	-
Trade creditors	3,272	6,482	1,604	-	-
Current Maturity of Long Term Loan	-	415	445	-	-
Accrued and other liabilities	439	288	973	1,100	1,251
<b>Current liabilities</b>	<b>11,024</b>	<b>15,641</b>	<b>6,903</b>	<b>3,116</b>	<b>3,186</b>
<b>Total liabilities</b>	<b>11,827</b>	<b>16,378</b>	<b>7,380</b>	<b>3,160</b>	<b>3,230</b>
<b>Total equity and liabilities</b>	<b>14,968</b>	<b>20,975</b>	<b>13,353</b>	<b>16,217</b>	<b>19,520</b>

Source: Company Projections, BMA Research

**Table 7: Cash Flows Statement**

PKR Mn	FY19	FY20	FY21E	FY22F	FY23F
Cash flows from operations	(575)	(918)	6,502	1,389	4,851
Cash flows from investing activities	(1,298)	1,347	(602)	(612)	(2,098)
Cash flows from financing activities	1,764	103	(5,750)	258	(2,550)
<b>Cash at the end of the year</b>	<b>391</b>	<b>282</b>	<b>964</b>	<b>1,998</b>	<b>2,202</b>

Source: Company Projections, BMA Research

**Biggest product portfolio:** Over the past few years, Air Link has increased its presence in the market by focusing more on partnering with key mobile operators in Pakistan.

Chart 1: Product portfolio

Partnership with all major brands



Source: Air Link Prospectus, BMA Research

IPO panned to raise PKR 5.85Bn

**Largest IPO in the history of Pakistan:** Air Link Communication (Pvt.) Limited which is set to become the largest IPO in Pakistan's history, intends to offer 90Mn shares (25% of its post paid up share capital) to the general public, in the form of 60Mn new shares and 30Mn offer-for-sale by the largest sponsor of the company, Mr. Muzzaffar Hayat Piracha. 75% of the IPO (67.5Mn shares) will be offered through the book building process and remainder 25% (22.5Mn shares) to retail investors. The post IPO shares of the company will increase to 360Mn (300Mn outstanding + 60Mn new shares). The Initial Public Offering (IPO) is set at a floor price of PKR 65.0/sh, with premium of 55.0/sh and the book building process is scheduled to commence from 30th August, 2021 where the strike price will be determined through Dutch auction method.

The smartphone market has grown at a 3 year CAGR of 22%

**The huge gap between the cellular and smart phone penetration is likely to spur organic growth:** The smart phone market has been constantly growing for the past few years in Pakistan with a 3-year CAGR of 21.9% over FY18-21. Despite the robust growth, cellular penetration in Pakistan has remained significantly higher at 84.2% compared to the smart phone penetration of only 18%. The huge gap between the cellular and smart phone users shows the immense potential of organic growth in smart phone space as cellular mobile operators are likely to phase-out their 2G networks as 4G becomes more widely available.

Company has delivered revenue/earnings growth of 49/30% over FY15-20

**Earnings momentum to continue:** Air Link Communication (Pvt.) Limited has achieved tremendous revenue/earning growth of 49/30% over FY15-20 due to its strong distribution network (16 regional hubs, 1,000+ wholesalers, 4,000+ retailers and coverage in 300+ cities). With the commencement of assembly line in Apr'21 and expansion plan of additional 150,000 units by FY23, we expect the company to post strong revenue/earnings CAGR of 28%/57% over FY21-25 respectively.

We recommend subscribing till the ceiling price of PKR 91/sh.

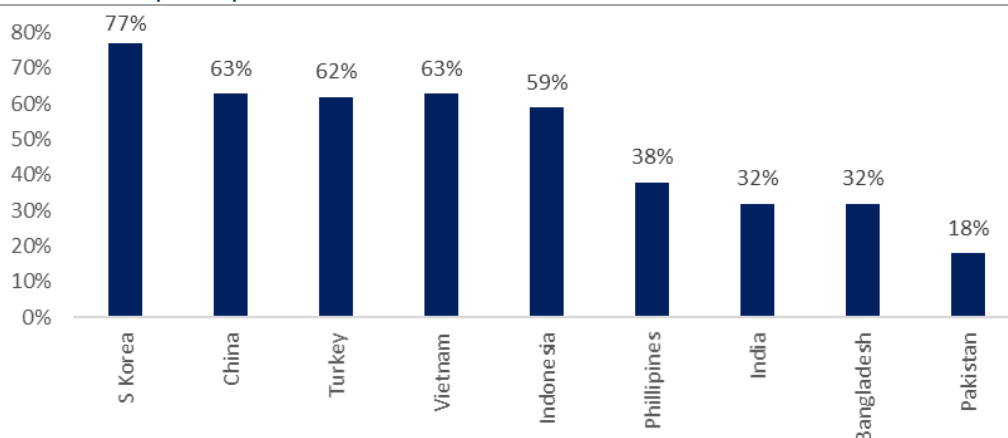
**Valuation:** Due to the unavailability of a similar business model in the listed space, we have assumed a discount of 45% to market weighted average P/E of 26.2x to arrive at our target P/E multiple of 11.8x. With FY22E earnings of PKR 10.2/sh, we arrive at our Jun'22 Target price of PKR 120/sh which entails a significant upside of 32% from the upper limit of PKR 91/sh. Hence, we recommend subscribing till the ceiling price of PKR 91/sh.

## Industry Overview & Analysis

Cellphone penetration has reached 86% in 2021

**Cellular penetration has increased to 86% over the past two decades:** Over the past two decades, mobile phone ownership grew at an astounding rate in Pakistan, with 86pc of the population now owning a cellphone, up from just 5pc in 2002. Whereas, smartphone penetration has remained low at 18% due to limited outreach of 3G/4G services. Note that Pakistan has the lowest smartphones penetration among regional countries.

Chart 2: Smartphone penetration in Pakistan (%)



Source: Air Link Prospectus, BMA Research

Increased conversion from feature phones to smartphones

**The trend is shifting towards smartphones:** However, the paradigm is shifting as smartphone prices decline (Cheapest smartphone priced at PKR 7,200), higher 3G & 4G subscriptions (100Mn in FY21), increased awareness and overall improved functions offered by smartphones. During Mar'21, around 1.3Mn smartphones were sold, with the mid-end segment (USD 100-300) commanding the lion's share at 73%. Given 100Mn 3G & 4G subscribers in the country and only 40% using smartphones, the total operational smartphones in the country are estimated to be 40Mn. Assuming a replacement cycle of 3 years, this results in annual demand of 13.3Mn.

Chart 3: Smartphone sales volume (Mn)

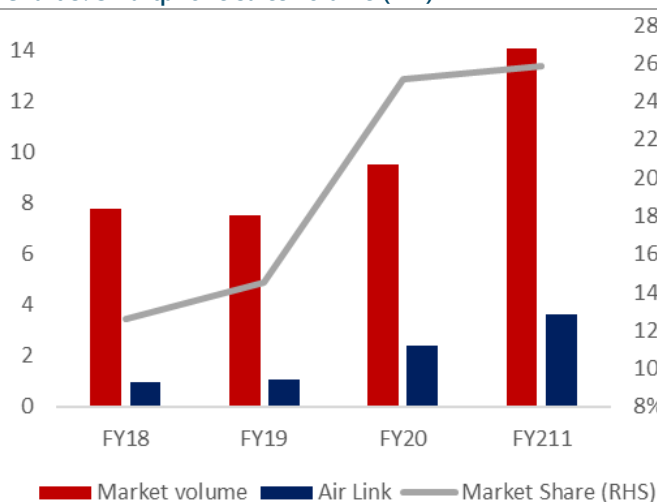
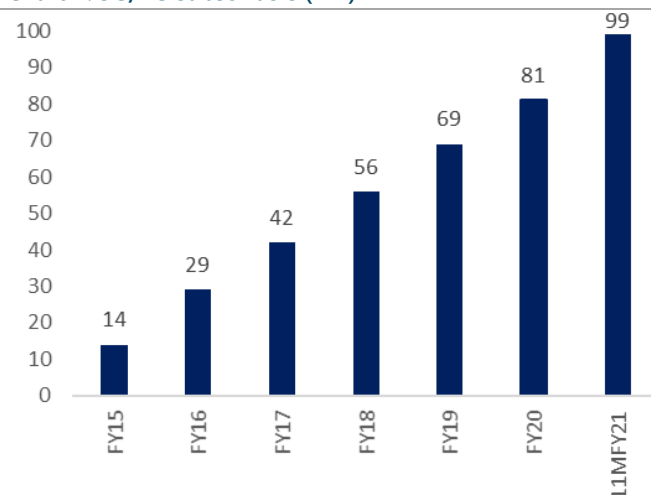


Chart 4: 3G/4G subscribers (Mn)

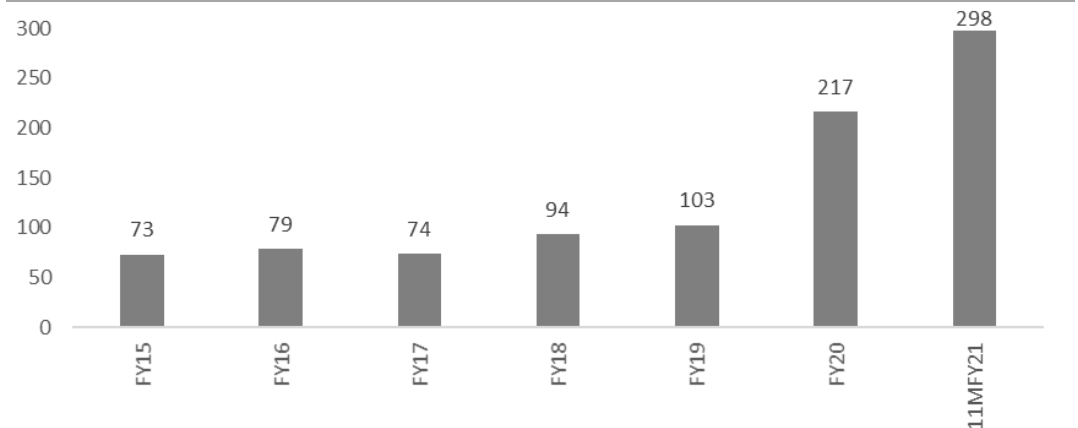


Source: PTA, BMA Research

Mobile imports increased by  
37% YoY in 11MFY21

**Mobile imports have increased to a massive PKR 297.8Bn in 11MFY21:** Pakistan's telecom sector witnessed significant growth after the introduction of 3G and 4G back in 2014. This in turn supported the growth of e-commerce industry and led to an increase in demand for smartphones. As of now, telecommunication companies in Pakistan have successfully completed testing of 5G technology. This presents a huge opportunity for smartphone growth. During FY15-20, the average annual mobile phone imports amounted to PKR 103.6Bn. And up to May'21, the total mobile phone imports have increased to PKR 297.8Bn, which represents an increase of 37% compared to last year.

**Chart 5: Pakistan mobile phone imports (PKR Bn)**



Source: Air Link Prospectus, BMA Research

Favorable demographics to  
boost industry growth

**What does the retail industry have on offer?** The smart phone industry is likely to benefit from a sharp recovery in economic growth, rising urbanization (Pakistan has the highest rate of urbanization of 36.4% in South Asia), which will help to expand the mid-income group, uplift spending and create space for smartphones purchases. An ongoing rise in female workforce participation will further boost house-hold income. E-commerce and particularly mobile e-commerce will notably see sales soar going forward which will further boost demand for smart phones, in our view. Furthermore, around one-third of the country's population is aged between 20 and 40 years (median age of 22.8) whose income levels are gradually rising. Since usage of mobile phones has transformed into a necessity, the smart phone industry is likely to benefit from the young population of Pakistan. The Implementation of DIRBS will also boost local demand as it continues to reduce the grey market and increases demand for registered devices.

**Table 8: Demographics of smartphone industry**

Population	212.8 million
Adults-Above 16 years (65% of Population)	138 million
Cellular Subscriber (Number of Sims)	183 million
3G/4G Subscribers (As of May 2021)	99 million
Provision of smartphones	35%
Smartphones	48 million
Lifecycle Replacement time	3 years
Smartphones-estimated annual demand	16 million

Source: Air Link Prospectus, BMA Research

Banking the unbanked customers likely to improve  
smartphone penetration

**Financial inclusion will help increase demand for smartphones in Pakistan:** The increasing usage of cellular mobile services in Pakistan has opened up new avenues of possibility by bringing the unbanked population into the banking channel. Moreover, the GoP is taking initiatives to digitize financial services that will facilitate the poor and marginalized sections of the society towards adopting digital payments while shifting the focus of banks from 'Over-the-Counter' (OTC) services to branchless banking/mobile wallets. These services are likely to increase usage of smartphones going forward, in our view.

## Transaction Structure & Company Analysis

90Mn shares on offer (25% of post paid up)

**IPO Transaction structure:** Air Link Communication (Pvt.) Limited which is set to become the largest IPO in Pakistan's history, intends to offer 90Mn shares (25% of its post paid up share capital) to the general public, in the form of 60Mn new shares and 30Mn offer-for-sale by the largest sponsor of the company, Mr. Muzaffar Hayat Piracha. 75% of the IPO (67.5Mn shares) will be offered through the book building process and remainder 25% (22.5Mn shares) to retail investors. The post IPO shares of the company will increase to 360Mn (300Mn outstanding + 60Mn new shares). The Initial Public Offering (IPO) is set at a floor price of PKR 65.0/sh, with premium of 55.0/sh and the book building process is scheduled to commence from 30th August, 2021 where the strike price will be determined through Dutch auction method.

Proceed will be used for working capital requirements

**Utilization of IPO proceeds:** IPO proceeds will mainly be used to fund working capital requirements of the company. The issuers' total working capital requirement is PKR 4,890Mn, of which 80% will be financed through the new issue (60Mn shares) and remaining 20% will be financed through short term financing facilities. The working capital funds will be used to purchase inventory of mobile devices from company vendors and will be sold through its robust distribution channel.

The company has posted 5 year revenue/earnings CAGR of 49/29% over FY16-21

**Earnings growth outlook, sales expectations & other assumptions:** Over the past few years, Air Link has increased its presence in the market by focusing more on its distribution network. The strategy to increase its presence all over Pakistan via strengthening of its distribution network has enabled the company to achieve remarkable 5-year revenue/earnings CAGR of 49/29% and we expect this trend to continue going forward. In our forecasts, we have assumed revenue/earnings to grow at a 5-year CAGR of 26%/49% over FY21-26 respectively.

**Offering discounted trailing multiples:** Air Link is one of a kind mobile retail giant in Pakistan which offers trailing P/E multiple of 15.8x (40% discount to local players) vs the market weighted industry average of 26.2x. In addition, the company also offers cheap trailing P/S multiple of 0.5x vs the industry weighted average multiple of 2.9x, depicting a discount of 83%.

Table 9: Offers cheap trailing multiples

Company	P/E	P/S	3 Yr Sales CAGR (FY17-20)
23-Aug-2021	x	x	%
Air Link	15.8	0.5	48%
NATF (Cons.)	22.7	1.4	20%
AGP	21.7	5.0	14%
GLAXO	15.1	1.5	2%
SRVI (Cons.)	19.2	0.8	14%
COLG	32.2	3.6	14%
IMAGE	33.9	2.3	26%
<b>Weighted Avg</b>	<b>26.2</b>	<b>2.9</b>	<b>13%</b>

\*Calculation is based on Jan-Dec 20 period

Source: Air Link Prospectus, BMA Research

### Key risk and triggers:

- **Key upside triggers:** 1) higher than expected sales in distribution business as new contracts are signed; 2) higher overall smartphone penetration due to economic recovery and greater income levels; and 3) increase in mobile phone import tariff.
- **Key downside triggers:** 1) Decline in distribution business due to non-renewal of existing contracts; 2) Lower than expected demand of mobile phones in the country; 3) Entry of new players in the distribution business, and 4) reduction in import duty on smartphones.

Lowest trailing P/E among regional players

**Post IPO multiples comparison with regional players:** Air Link is one of a kind mobile retail brand in Pakistan and will be the only listed mobile phone industry player at PSX. In addition to core value generation, it also trades at a sizable 19% discount to foreign mobile retailers based on FY21 P/E multiple of 15.7x. Despite lower smartphone penetration in Pakistan, Air Link Communication (Pvt.) Limited has outperformed regional players in terms of revenue growth due to its strong branch network. As per data provided by the World Bank, Pakistan has the lowest tele-density (cellular subscriptions per 100 people) of 76.4% compared to the Egypt (95.0%) and Vietnam (141.2%), which shows huge potential of smartphones market in Pakistan.

**Table 10: Regional Telecommunication comparable multiples**

Company	Country	Country multiple	Trailing P/E	3yr Sales CAGR (FY 17-20)	Smartphone penetration	Tele-density (per 100 people)
<b>23-Aug-21</b>			<b>x</b>	<b>%</b>	<b>%</b>	<b>%</b>
Air Link	Pakistan	7.3	15.70	48%	18%	76.4
MWG	Vietnam	15.7	18.29	20%	45%	95.0
MTIE	Egypt	9.9	16.01	11%	28%	141.2

Source: Air Link Prospectus, BMA Research

Offers P/E multiple of 15.8x and 22.1x at floor and ceiling price

**IPO's trailing P/E multiple analysis:** Air Link offers P/E multiple of 15.8x and 22.1x at floor and ceiling price of PKR 65/sh and PKR 91/sh respectively, which is relatively higher compared to the other IPOs. The higher multiple for Air Link is justified given the company's ability to capitalize on growing demand due to the strong distribution network and vertically integrated business model.

**Table 11: IPO multiples in 2021**

Date of IPO	Company	Floor	Ceiling	Strike
27-Jan-21	PTL	7.5	10.6	10.6
7-Apr-21	SGF	11.0	15.3	15.3
15-Jun-21	CPHL	15.3	21.5	17.5
22-Jun-21	PABC	20.7	29.0	29.0
<b>30-Aug-21</b>	<b>Air Link</b>	<b>15.8</b>	<b>22.1</b>	<b>N/A</b>

Source: BMA Research

**Why do we like Air Link?** We recommend subscribing till the ceiling price of PKR91/sh, which comes to FY22 P/E of 8.9x. The company has no direct match on the bourse, therefore, we have applied a 45% discount to the weighted average industry P/E of 26.2x to calculate a target P/E multiple of 11.8x. Based on this target multiple, our FV estimate for the company comes out to PKR 120/sh.

- Air Link Communication (Pvt.) Limited is an exceptional growth story with multiple growth avenues such as consumer transition of shifting from cellular phones to low cost smart phones, overall economic recovery, and curbs on the grey market by PTA.
- Air Link Communication (Pvt.) Limited has become completely vertically integrated by commencing operations of its own assembly plant. Overall gross margins are stable, owing to adjustment in pricing provided by the vendors. Margins are likely to go up gradually as the company moves up and down the distribution chain.
- The Manufacturing SKDs in own assembly unit can result in potential duty savings in the range of 20-25% which will increase the demand for locally assembled phones.
- The company's e-commerce platform (www.airlink.pk) is also expected to increase the customer outreach by enabling online sales of smart phones.



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Buy	>15% expected total return
Hold	10%-15% expected total return
Underperform	<10% expected total return
*Total stock return = capital gain + dividend yield	

### Old rating system

Overweight	Total sector return > expected market return
Marketweight	Expected market return
Underweight	Total stock return < expected market return

## Valuation Methodology

To arrive at our period end target prices, BMA Capital uses different valuation methodologies including

- Discounted cash flow (DCF, DDM)
- Relative Valuation (P/E, P/B, P/S etc.)
- Equity & Asset return based methodologies (EVA, Residual Income etc.)