

Worldlink Communications Limited

Ratings

Facilities	Amount (Rs. Million)	Rating ¹	Rating Action
Long Term Bank Facilities-Term Loan	2,181.53	CARE-NP A [Single A]	Reaffirmed
Short Term Bank Facilities	3,010.00	CARE-NP A2+ [A Two Plus]	Reaffirmed
Total	5,191.53 Five Thousand One Hundred Ninety-One Million and Five Hundred Thirty Thousand Only)		

Annexure-1 Details of Facilities/Instruments to be rated

CARE Ratings Nepal Limited (CRNL) has reaffirmed the ratings of 'CARE-NP A' assigned to the long-term bank facilities and 'CARE-NP A2+' assigned to the short term bank facilities of Wordlink Communications Limited (WCL).

Detailed Rationale & Key Rating Drivers

The ratings assigned to WCL continues to derive strength from its established track record of operations, strong brand presence in Internet Service Provider (ISP) industry being the market leader supported by steady growth in its subscriber base over the period, experienced board and management team in the related field, investment from strong institutional shareholders, and wide portfolio of services offering reasonable revenue visibility. The ratings also factor in WCL's satisfactory financial profile marked by growth in operating income with healthy profitability margins and comfortable capital structure with adequate debt coverage indicators during FY22 (Audited, FY refers to the twelve-month period ending mid-July). The ratings also factor in WCL's, increased efforts for market penetration with latest technology and resources to increase outreach.

The ratings are, however, constrained by high capital and technology intensive nature of the ISP industry and requirement for regular investments for network expansion. The ratings also factor in increasing competition in the industry with fragmented market leading to moderation in profitability amid increasing pricing pressure, working capital intensive nature of operations, exposure to foreign exchange fluctuation risk, susceptibility to regulatory changes and technological risk associated with the ISP business.

Going forward, the ability of the company to maintain the growth in scale with sustained profitability while maintaining capital structure will remain the key rating sensitivities. Also, the ability of the company to withstand the increasingly competitive business environment in internet business and maintain market share as well as any substantial debt funded capital expenditure impacting the overall financial risk profile of the company will also remain the key rating sensitivities.

Detailed Description of the Key Rating Drivers

Key Rating Strengths

Experienced board and management team

WCL has five experienced directors on its board led by Mr. Dileep Agrawal, Chairman and Managing Director of the company. Mr. Agrawal completed his graduation in 1996 from Bates College, Maine, United States and is the promoter of the company who conceptualized WCL. He is responsible for overall corporate management and development of the company. Mr. Manoj Kumar Agrawal and Mr. Bijay Kumar Jalan are the Executive Directors of the company and are associated with WCL since inception. Mr. Arun S Korati is a representative Director on the Board from CDC Group. The Directors of the Company are aptly supported by a team of experienced professionals. Mr. Jashisha Kumar Gupta (Chief Financial Officer & Company/Board Secretary), Mr. Keshav Nepal (Chief Executive Officer) and Mr. Samit Jana Thing (Chief Technical Officer) are the Key Managerial Personnel of the Company, with substantial experience in the related field.

¹Complete definition of the ratings assigned are available at www.careratingsnepal.com and other CARE publications

Support from strong institutional shareholders, fresh infusion in FY23

WCL has received series B investment of Rs. 1,080 Mn from British International Investment and Rs. 900 Mn from Dolma Impact Fund in March 2023. With this, the total equity infusion through FDI in the company has reached Rs. 3,330 Mn. The amount received as FDI is being utilized in expanding the network infrastructure of the company. CDC is UK's development finance institution, wholly owned by the UK Government. CDC has investments in over 1,500 businesses in emerging economies with total net assets of £8.1bn. Dolma Impact Fund is an institutional investor and is the first commercial impact fund setup in Nepal for providing growth capital to Small and Medium Enterprises (SMEs) with strong entrepreneurial and management capacities.

Long track record of operations and strong reach and brand presence in ISP service

WCL has been operational in Nepal for over 25 years and is currently the leading ISP company operating in the country. The company occupies over 29% market share in the retail ISP segment in the country with active subscriber base of around 7.72 lakhs as on mid-April, 2023. WCL carries over 40% of the country's Internet bandwidth and has widespread coverage covering 70 plus districts and has 10,000 plus enterprise circuits connected to offices and organizations. The company has 88 branches across Nepal. Furthermore, WCL has established network infrastructure in 150 new locations in FY23 and plans to further expand in additional locations in the coming years.

Sustained leadership position in market backed by steady growth in subscriber base, albeit with decline in ARPU

WCL is Nepal's largest Internet Service Provider. As per the report published by Nepal Telecommunications Authority, total internet subscriber base of Nepal was 2,673,471 as on mid-April 2023, out of which WCL occupies 29% market share with subscriber base of 771,462 subscribers. WCL is the market leader in internet subscriber base of Nepal in fiber segment, with ~30% of market share. However, Average Revenue per Unit (ARPU) of the company has declined to Rs. 1,206 per user in FY22 from Rs. 1,123 per user in FY21 on account of various promotional packages and discounts offered to add subscriber base owing to the increased competition in the industry. Given its established brand presence, the company continues to drive in better ARPUs vis-à-vis competition. Going forward, ARPU levels are likely to remain muted which might have a bearing of on the company's profitability over the near-term. However, this is expected to be offset to some extent by cost advantage arising from economies of scale over the medium term.

Satisfactory financial risk profile

During FY22, WCL's Total Operating Income increased by 18.07% year-on-year (y-o-y) to Rs. 9,391 Mn, backed by growing subscriber base, which grew by ~29% y-o-y to 660,202 amid increasing market penetration and surge in demand for internet in the industry. Profitability of the company continues to remain healthy vis-à-vis peers although with some moderation in FY22 on account of increased expenditure for promotion of business and on account of increased capex leading to various additional fixed expenditure incurred and charged to business. Similarly, PAT margin declined to 5.10% in FY22 from 11.52% in FY21 owing to increased finance cost related to fresh debt draws for capex.

Revenue growth trend has continued into 9MFY23 with the company reporting income of Rs. 8,210 Mn (9MFY22: Rs. 6,274 Mn). Margins are expected to remain rangebound with increased operating expenses related to ongoing capex for network expansion likely to be offset by benefits from increasing scale.

Comfortable capital structure and debt coverage indicators

WCL has been undertaking setting up network infrastructures in new locations in FY22-FY23 to improve its market penetration. Amid increased debt for the capex, the company's debt to equity ratio had deteriorated to 1.70x at the end of FY22 from 0.34x at the end of FY21 and overall gearing ratio of the company also shot up to 1.88x at the end of FY22 from 0.46x at the end of FY21. However, boosted by the equity infusion of Rs. 1,980 Mn in March 2023, the company's debt to equity and overall gearing ratio have improved to 0.76x and 0.98x, respectively, as on mid April 2023. Furthermore, coverage indicators in FY22 also moderated on a y-o-y basis

owing to increased debt levels at FY22 end. During FY22, the company's interest coverage ratio had declined to 12.14x (FY21:36.69x) and total debt to GCA ratio stood at 2.94x (FY21:1.51x). Debt coverage indicators of the company are likely to improve going forward following the repayment of loans in FY23 from the proceeds of the FDI. Capital structure is expected to remain fairly steady with impact of additional debt likely to be offset by accretion of profits. Any higher than envisaged debt levels leading to material deterioration in the company's capital structure will remain key monitorable from analytical perspective.

Diversified portfolio of services offering revenue visibility

WCL offers a wide array of services to a well-diversified client base and revenue ISP services is a major component of the total income. The company reported 42% of its revenues in FY22 from retail customers in ISP Service, 7% from corporate customer in ISP Service. Although ISP constitutes the major component of total income, the company also books sizeable revenues from monitoring and technical support, data connectivity and other sales. WCL has managed to maintain its dominant market share in Nepal and also increase its subscription revenues. The ability of company to retain the acquired customers, thereby reducing churn through competitive pricing and content offering while maintaining its profitability would be key to its future prospects.

Latest technology and resources to increase outreach

WCL is the pioneer in fiber connectivity in Nepal and is the first private company in the country to connect through satellite. It is also the first company to have its own wireless trunk network. WCL introduced FTTH (Fiber to the Home) technology in 2012, after years of research. In 2018, the company announced a partnership with the Finnish multinational IT infrastructure firm Nokia to expand its FTTH network to reach out to one million Nepali households. Till date, the length of its fiber network across the country totals 13,646 kms. WCL's updated technology makes it capable of competing globally because of the same technological parity.

It is the first company in Nepal to update its network to XGS-PON. With this innovation, the company will be able to provide more than 1Gbps connection to its customer in coming days. As of late, WCL has introduced Nokia Wi-Fi Beacon the in-home router with built-in insights screens. Its predominant innovation guarantees unmatched Wi-Fi scope and ensures high-speed web association on each gadget. WCL's upgraded innovation makes it competent of competing all-inclusive since of the same innovative equality.

Key Rating Weakness

High capital and technology intensive nature of industry

It is an inherent nature of telecom industry which requires high capital investments and long gestation period necessitating substantial funding support. Currently, WCL's fiber network is mostly concentrated to major cities with dense population. In order to increase its footprint WCL is planning to roll out additional fiber coverage on their network. Rolling out fiber network in remote areas of Nepal is a capital-intensive business. Similarly, to order to increase the outreach in uncovered area, the company has established network infrastructure in 150 new locations in FY23, for which significant capital expenditures has been incurred, which were funded through additional debt and internal accruals. To remain competitive in the ISP business, substantial capital expenditures is a necessity going forward as well. The company's ability to arrange a judicious mix of equity and debt funding for its capex need in the future remains critical from credit perspective. Substantial outside debt to fund the future capex could translate to moderation of debt coverage indicators.

Increasing competition in the industry with fragmented market

With increasing digitization, number of ISPs in the country has increased significantly. As on mid-April 2023, there were 63 licensed ISPs operating in Nepal with total internet subscriber base of 2,673,471 which has increased from 58 ISPs with subscriber base of 1,659,306 at the end of FY21. The competitors for WCL's internet and related network services include not only other internet service providers, but also existing telecommunications companies planning to increase their presence in the segment. Predatory pricing of any new entrant in this segment may adversely impact WCL's market share and APRU levels. Also, currently the ISP industry in Nepal is fragmented with numerous smaller unorganized players active in small pockets of the market. In order to meet customer

expectation of availing internet in low pricing, the prices have come down steadily over the past 2-3 years, thereby affecting the margins of ISPs. Many competitors' resort to predatory pricing in order to poach customers. WCL's market share has moderated from 34% at FY20 end, to 29% at the end of 9MFY23 although, in absolute terms, WCL's subscriber base has increased at a CAGR of around ~74% over FY20-9MFY23.

Working capital intensive nature of operations and exposure to foreign exchange fluctuation risk

The operations of the company are working capital intensive in nature. The company is required to make huge invest in customer premises equipment (CPE) and other accessories. Generally, WCL imports CPEs which are backed by letter of credit (LC), however full recovery of the same from the customers happen on due course of time which results into high reliance on working capital loans. During FY22, WCL had inventory turnover of 141 days and debtor's turnover of 13 days with creditor turnover of 115 days. Due to high creditor days, operating cycle of the company is low at 39 days in FY22. This all led to working requirement, which was met to bank borrowing.

Furthermore, the CPE installed at the subscribers' premise are majorly imported from China and payment is done in foreign currency. The procurement of CPEs which is positively correlated with the growth in subscriber base leads to large outflow of forex. WCL has no earnings in foreign currency, however the company manages its foreign currency risk by not holding the payables in foreign currency for longer duration. However, the company currently partially hedges its foreign currency exposures by executing forward contracts to minimize risk of foreign exchange fluctuations. During FY22, WCL booked net foreign exchange loss of Rs. 111 Mn as compared to Rs. 16 Mn in FY21.

Susceptibility to regulatory changes

The cost of infrastructure provided by the government to ISP's is on increasing trend. Effective from mid-July 2019, the Nepal government levied Telecommunication Service Charge (TSC) of 10% on internet subscription in addition to the existing 13% Value Added Tax (VAT). The newly levied service charge was adjusted in the cost of the ISP's without increasing the consumer prices. Further, in August 2019, Nepal Electricity Authority (NEA) has sought to hike the fee for its infrastructure being used by the ISPs, which is likely to take upward the cost of internet use. WCL along with other ISPAN (Internet Service Providers of Nepal) members have not accepted the proposed rate and hence due to this disagreement, NEA has not raised any invoice in the previous and current financial year. Government of Nepal has set up a High-Power Committee in order to resolve the issue. Also, company has been booking expenses on the basis of previously raised invoices by NEA and in the event if the decision is in favor of NEA the impact on the financial profile of the company is expected to be minimal.

Technological risk associated with ISP business.

Technology related companies are in particular prone to obsolescence risk and their revenues can be significantly affected with technology risk wherein the end users migrate from obsolete technologies to most recent technology. Therefore, this risk remains a concern for the company, if company is not able to timely upgrade itself to latest technologies. New technology may have short lifecycle considering the continued spend on Research & Development and faster adoption of new technologies. Any change in technology may impact the operations of the broadband industry. However, WCL has been continuously involved in research and development activities to on-board new technologies in Nepal.

About the Company

Worldlink Communications Limited (WCL) was incorporated on January 21, 1996 as a private limited company and later converted to public limited company on April 24, 2019. WCL is Nepal's largest Internet Service Provider with 25 years in the industry under the brand name of 'Worldlink'.

Brief Financials of the company during last 3 years is as under

(in Rs. Million)

For the year ended mid-July	FY20	FY21	FY22
	Audited	Audited	Audited
Income from Operations	6,545	7,954	9,391
PBILDT Margin	35.14	37.14	33.06
Overall Gearing (times)	0.89	0.46	1.88
Interest coverage (times)	13.45	36.69	12.14
Current ratio (times)	1.34	1.20	1.06
Total Debt/GCA	0.61	0.41	2.94

Annexure-1 Details of Facilities/Instruments to be rated

Name of Instrument	Type of Facility	Amount (Rs in Million)	Rating
Long Term Bank Facilities	Working Capital Loans	2,181.53	CARE-NP A
Short Term Bank Facilities	Fund Based	140.00	CARE-NP A2+
Short Term Bank Facilities	Non-Fund Based	2,870.00	CARE-NP A2+
Total		5,191.53	

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