The Pakistan Credit Rating Agency Limited

Rating Report

Engro PowerGen Thar (Pvt.) Limited

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Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
27-Jun-2018	A	A1	Stable	Maintain	-
22-Dec-2017	A	A1	Stable	Maintain	-
21-Jun-2017	A	A1	Stable	Maintain	-
30-Dec-2016	A	A1	Stable	Initial	-

Rating Rationale and Key Rating Drivers

Engro Powergen Limited (EPL) along with China Machinery & Engineering Corporation (CMEC) is setting up first Thar coal based (2 x 330 MW) power plant (Complex) - Engro Powergen Thar (Pvt.) Limited (EPTL). The project achieved financial close (FC) in Apr-16 and the project's contracted COD is in Oct-19. However, management is aiming for COD in Jun-19 on best efforts basis. RCOD is Jun-19 as per PPA and delay LDs will apply if this date is exceeded. Nevertheless, in case of any delays, LDs will be paid through shareholders' ROE. The primary fuel is Thar Coal; however, the plant can accommodate imported coal. A 30 year coal supply agreement is signed with Sindh Engro Coal Mining Company (SECMC), which is constructing a coal mine in Thar Block-II. The mine's contracted COD is Oct-19, though the management is targeting COD by June-19. As of May-18, the actual progress is 84.7% based on the shorter 38-month schedule. The financial strength and experience in energy chain of the sponsoring companies – EEL and CMEC – is positive to the ratings. The onshore EPC contract is with CERIECO and offshore EPC contract is with CMEC. Comfort is drawn from the experience of these contractors and the involvement of Pakistan and Chinese governments, as this project comes under CPEC. The ratings incorporate the project's exposure to the completion risks of multiple affiliated infrastructure projects needed for the successful commissioning of the Complex. Once completed, the Company's main challenge would be to keep the plant operational. Off take agreement is with NTDC, which will, upon plant's availability as per contract, provide capacity payments even if no purchase order is placed. The Government of Pakistan has given payment guarantee against dues from NTDC. The business risk of the company is exposed to the specifications of Thar Coal, which is being used for the first time. However, use of CFB Boiler by the Company largely covers the risk of varying lignite quality.

The management's ability to effectively manage EPC risks provides comfort. Ensuring timely commissioning of the project would remain critical, which, once achieved, would be ratings positive. Moreover, timely completion of the affiliated infrastructure projects needed to make the plant operational and the viability of Thar Coal is critical. External factors such as any adverse changes in the regulatory framework or material delay in achieving CoD may impact the ratings.

Disclosure

Name of Rated Entity	Engro PowerGen Thar (Pvt.) Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology | Corporate Rating Methodology(Jul-17),Methodology | Correlation between long-term and short-term rating scale(Jun-17),Methodology | Criteria Modifiers(Jun-17)
Related Research	Sector Study | Power(Apr-18)
Rating Analysts	Muhammad Hassan | muhammad.hassan@pacra.com | +92-42-35869504

EPTL PROFILE	
Incorporated	2014
Major business lines	Independent Power Producer
Legal status	Public Limited
Expected COD	June 2019
Plant Specifications	2*330 MW
Primary Fuel	Coal
Plant Location	Thar, Sindh
Head Office	Karachi

INDUSTRY SNAPSHOT

- Pakistan total power generation is increasing on the back of new power projects under CPEC
- Pakistan's energy mix is shifting towards Gas/RLNG and coal from Furnace Oil and other expensive sources
- Gas fired power plants have lowest per unit cost among all fossil fuel power plants.
- Going forward, cheap renewable electricity will be a challenge to viability of Thermal power plants.

OWNERSHIP

- EPTL's majority ordinary shares are owned by Engro Energy Limited (EEL) (50.1%) and China Machinery Engineering Company (CMEC) (35%).
- The remaining stake is owned by Habib Bank Limited (HBL) (9.5%) and Liberty Mills Limited (LML) (5.4%). In addition to ordinary shares, $85mln preference shares are all subscribed by CMEC.

GOVERNANCE

- BoD comprises nine members including the CEO; five represent EEL, three CMEC and one HBL.
- Mr. Shamsudin, Ex CEO is now the Chairman of the Board.
- Diverse experience of the Board Members over different industries is a comforting factor.

MANAGEMENT

- Mr. Ahsan Zafar Syed, CEO of EPTL, He has ample experience in engineering, procurement & construction management, and project management. He was previously engaged with EPTL as Chief Operating Officer.
- Mr. Ahsan is accompanied by a lean but efficient management team.

COMPLETION RISK

- EPTL has signed an Onshore EPC agreement with China East Resource Import & Export Co. (CERIECO) and an offshore agreement with CMEC.
- CERIECO, established in 1993 is a Chinese state-owned company. It specializes in EPC contracts and engineering consulting services
- CMEC, since 1978, provides engineering consulting, project design, financing solutions, and plant logistic services locally and internationally.
- The RCOD of the Complex is June-2019 while contracted COD is Oct-2019. In case of any delays, LDs will be paid through shareholders' ROE.
- Coal Supply Agreement has been signed with Sindh Engro Coal Mining Company (SECMC) and the mine's contracted COD is Oct-2019.
- The successful commissioning and operations of the Complex, in addition to its own completion, is dependent on mine's COD and other affiliated infrastructure projects.
- Other affiliated infrastructure projects are; Water Supply System, Effluent Disposal Scheme, Transmission Line, Road Network, & Airport. These projects are to be completed by Government of Sindh & Government of Pakistan. Expected completion of these projects is end-2018.
- As of May-18, the actual progress is 84.7%, based on the shorter 38-month schedule.
- EPTL has attained reasonable insurance cover for material damage, third party liability, and delay in startup affecting the profits. Additionally, Marine, Terrorism, and Excess Third Party Liability Insurances are also held.

PERFORMANCE

- EPTL has amended its O&M Contractor. Now the O&M contract has been signed with EPSH with 10 year contract period.
- Contracted availability and efficiency is 85% and 37% respectively.
- The ROE provided to EPTL on use of Thar coal is 30.65% & 24.5% on imported coal.

FINANCIAL RISK

- Debt financing constitutes 75% of the project cost; $831mln.
- USD facility of $621mln and local facility of $210mln have a 14 year door to door tenure, and are to be paid in 20 semi-annual payments over a period of 10 years after COD. The USD facility is at LIBOR + 4.2% and local at KIBOR + 3.5%.
- The yearly debt and mine capacity payments can be made at 67% availability (8 months of availability).

PKR mln

Engro Powergen Thar (Pvt.) Limited

BALANCE SHEET	31-Mar-18	31-Dec-17	31-Dec-16	31-Dec-15
	3M	Annual	Annual	Annual
Non-Current Assets	**62,464**	**56,985**	**31,497**	**1,576**
Investments (Others)	**-**	**-**	**-**	**-**
Current Assets	**5,234**	**3,870**	**1,336**	**294**
Trade Receivables	-	-	-	-
Other Current Assets	149	124	55	6
Cash & Bank Balances	5,085	3,746	1,282	288
TOTAL ASSETS	**67,698**	**60,855**	**32,833**	**1,870**
Debt	**44,196**	**38,634**	**14,440**	**-**
Short-term	-	-	-	-
Long-term (Inlc. Current Maturity of long-term debt)	44,196	38,634	14,440	-
Other Short term liabilities (inclusive of trade payables)	2,471	1,162	2,165	91
Other Long term Liabilities	-	-	-	-
Shareholder's Equity	**21,031**	**21,059**	**16,228**	**1,778**
TOTAL LIABILITIES & EQUITY	**67,698**	**60,855**	**32,833**	**1,870**

INCOME STATEMENT				
Admin Expenses	(8)	(25)	(36)	(14)
Other Income	-	-	21	10
Financial Charges	-	-	(0)	-
Taxation	(0)	(0)	(1)	(0)
Net Income	**(8)**	**(25)**	**(16)**	**(4)**

Cashflow Statement				
Free Cashflow from Operations (FCFO)	80	(57)	(19)	(13)
Net Cash changes in Working Capital	522	(1,355)	1,810	77
Net Cash from Operating Activities	602	(1,413)	1,792	64
Net Cash from InvestingActivities	(3,241)	(25,004)	(22,950)	(462)
Net Cash from Financing Activities	3,981	28,883	22,145	565
Net Cash generated during the period	1,339	2,464	994	171

Ratio Analysis				
Capital Structure (Total Debt/Total Debt+Equity)	67.7%	68.4%	47.0%	0.0%

Rating Scale

Credit Rating Scale & Definitions

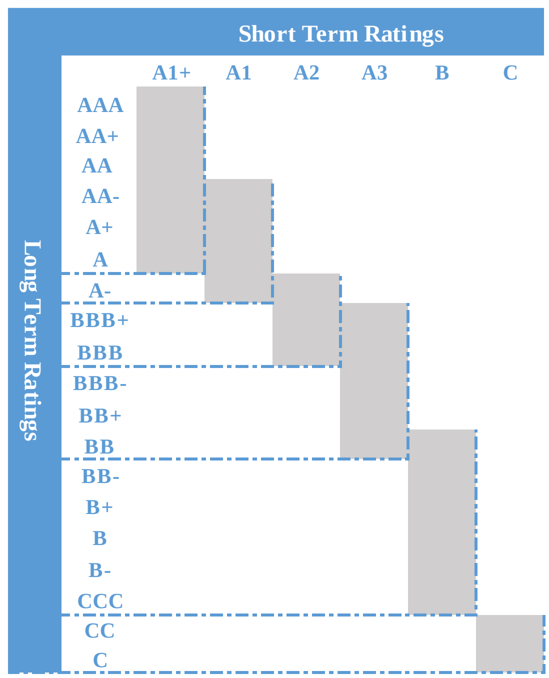
Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

Long Term Ratings

AAA	**Highest credit quality.** Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments
AA+ AA AA-	**Very high credit quality.** Very low expectation of credit risk. Indicate very strong capacity for timely payment of financial commitments. This capacity is not significantly vulnerable to foreseeable events.
A+ A A-	**High credit quality.** Low expectation of credit risk. The capacity for timely payment of financial commitments is considered strong. This capacity may, nevertheless, be vulnerable to changes in circumstances or in economic conditions.
BBB+ BBB BBB-	**Good credit quality.** Currently a low expectation of credit risk. The capacity for timely payment of financial commitments is considered adequate, but adverse changes in circumstances and in economic conditions are more likely to impair this capacity.
BB+ BB BB-	**Moderate risk.** Possibility of credit risk developing. There is a possibility of credit risk developing, particularly as a result of adverse economic or business changes over time; however, business or financial alternatives may be available to allow financial commitments to be met.
B+ B B-	**High credit risk.** A limited margin of safety remains against credit risk. Financial commitments are currently being met; however, capacity for continued payment is contingent upon a sustained, favorable business and economic environment.
CCC CC C	**Very high credit risk.** Substantial credit risk "CCC" Default is a real possibility. Capacity for meeting financial commitments is solely reliant upon sustained, favorable business or economic developments. "CC" Rating indicates that default of some kind appears probable. "C" Ratings signal imminent default.
D	Obligations are currently in default.

Short Term Ratings

A1+	The highest capacity for timely repayment.
A1	A strong capacity for timely repayment.
A2	A satisfactory capacity for timely repayment. This may be susceptible to adverse changes in business, economic, or financial conditions.
A3	An adequate capacity for timely repayment. Such capacity is susceptible to adverse changes in business, economic, or financial conditions.
B	The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions.
C	An inadequate capacity to ensure timely repayment.



Outlook (Stable, Positive, Negative, Developing) Indicates the potential and direction of a rating over the intermediate term in response to trends in economic and/or fundamental business/financial conditions. It is not necessarily a precursor to a rating change. 'Stable' outlook means a rating is not likely to change. 'Positive' means it may be raised. 'Negative' means it may be lowered. Where the trends have conflicting elements, the outlook may be described as 'Developing'.

Rating Watch Alerts to the possibility of a rating change subsequent to, or in anticipation of, a) some material identifiable event and/or b) deviation from expected trend. But it does not mean that a rating change is inevitable. A watch should be resolved within foreseeable future, but may continue if underlying circumstances are not settled. Rating Watch may accompany Outlook of the respective opinion.

Suspension It is not possible to update an opinion due to lack of requisite information. Opinion should be resumed in foreseeable future. However, if this does not happen within six (6) months, the rating should be considered withdrawn.

Withdrawn A rating is withdrawn on a) termination of rating mandate, b) cessation of underlying entity, c) the debt instrument is redeemed, d) the rating remains suspended for six months, e) the entity/issuer defaults., or/and f) PACRA finds it impractical to surveill the opinion due to lack of requisite information.

Harmonization A change in rating due to revision in applicable methodology or underlying scale.

Rating Team Statements
(1) Rating is just an opinion about the creditworthiness of the entity and does not constitute recommendation to buy, hold or sell any security of the entity rated or to buy, hold or sell the security rated, as the case may be | Chapter III; 14-3-(x)

2) **Conflict of Interest**
i. The Rating Team or any of their family members have no interest in this rating | Chapter III; 12-2-(j)
ii. PACRA, the analysts involved in the rating process and members of its rating committee, and their family members, do not have any conflict of interest relating to the rating done by them | Chapter III; 12-2-(e) & (k)
iii. The analyst is not a substantial shareholder of the customer being rated by PACRA [Annexure F; d-(ii)] Explanation: for the purpose of above clause, the term "family members" shall include only those family members who are dependent on the analyst and members of the rating committee

Restrictions
(3) No director, officer or employee of PACRA communicates the information, acquired by him for use for rating purposes, to any other person except where required under law to do so. | Chapter III; 10-(5)
(4) PACRA does not disclose or discuss with outside parties or make improper use of the non-public information which has come to its knowledge during business relationship with the customer | Chapter III; 10-7-(d)
(5) PACRA does not make proposals or recommendations regarding the activities of rated entities that could impact a credit rating of entity subject to rating | Chapter III; 10-7-(k)

Conduct of Business
(6) PACRA fulfills its obligations in a fair, efficient, transparent and ethical manner and renders high standards of services in performing its functions and obligations; | Chapter III; 11-A-(a)
(7) PACRA uses due care in preparation of this Rating Report. Our information has been obtained from sources we consider to be reliable but its accuracy or completeness is not guaranteed. PACRA does not, in every instance, independently verifies or validates information received in the rating process or in preparing this Rating Report.
(8) PACRA prohibits its employees and analysts from soliciting money, gifts or favors from anyone with whom PACRA conducts business | Chapter III; 11-A-(q)
(9) PACRA ensures before commencement of the rating process that an analyst or employee has not had a recent employment or other significant business or personal relationship with the rated entity that may cause or may be perceived as causing a conflict of interest; | Chapter III; 11-A-(r)
(10) PACRA maintains principal of integrity in seeking rating business | Chapter III; 11-A-(u)
(11) PACRA promptly investigates, in the event of a misconduct or a breach of the policies, procedures and controls, and takes appropriate steps to rectify any weaknesses to prevent any recurrence along with suitable punitive action against the responsible employee(s) | Chapter III; 11-B-(m)

Independence & Conflict of interest
(12) PACRA receives compensation from the entity being rated or any third party for the rating services it offers. The receipt of this compensation has no influence on PACRA´s opinions or other analytical processes. In all instances, PACRA is committed to preserving the objectivity, integrity and independence of its ratings. Our relationship is governed by two distinct mandates i) rating mandate - signed with the entity being rated or issuer of the debt instrument, and fee mandate - signed with the payer, which can be different from the entity
(13) PACRA does not provide consultancy/advisory services or other services to any of its customers or to any of its customers' associated companies and associated undertakings that is being rated or has been rated by it during the preceding three years unless it has adequate mechanism in place ensuring that provision of such services does not lead to a conflict of interest situation with its rating activities; | Chapter III; 12-2-(d)
(14) PACRA discloses that no shareholder directly or indirectly holding 10% or more of the share capital of PACRA also holds directly or indirectly 10% or more of the share capital of the entity which is subject to rating or the entity which issued the instrument subject to rating by PACRA; | Reference Chapter III; 12-2-(f)
(15) PACRA ensures that the rating assigned to an entity or instrument is not be affected by the existence of a business relationship between PACRA and the entity or any other party, or the non-existence of such a relationship | Chapter III; 12-2-(i)
(16) PACRA ensures that the analysts or any of their family members shall not buy or sell or engage in any transaction in any security which falls in the analyst's area of primary analytical responsibility. This clause shall, however, not be applicable on investment in securities through collective investment schemes. | Chapter III; 12-2-(l)
(17) PACRA has established policies and procedure governing investments and trading in securities by its employees and for monitoring the same to prevent insider trading, market manipulation or any other market abuse | Chapter III; 11-B-(g)

Monitoring and review
(18) PACRA monitors all the outstanding ratings continuously and any potential change therein due to any event associated with the issuer, the security arrangement, the industry etc., is disseminated to the market, immediately and in effective manner, after appropriate consultation with the entity/issuer; | Chapter III | 18-(a)
(19) PACRA reviews all the outstanding ratings on semi-annual basis or as and when required by any creditor or upon the occurrence of such an event which requires to do so; | Chapter III | 18-(b)
(20) PACRA initiates immediate review of the outstanding rating upon becoming aware of any information that may reasonably be expected to result in downgrading of the rating; | Chapter III | 18-(c)
(21) PACRA engages with the issuer and the debt securities trustee, to remain updated on all information pertaining to the rating of the entity/instrument; | Chapter III | 18-(d)
Probability of Default
(22) PACRA´s Rating Scale reflects the expectation of credit risk. The highest rating has the lowest relative likelihood of default (i.e, probability). PACRA´s transition studies capture the historical performance behavior of a specific rating notch. Transition behavior of the assigned rating can be obtained from PACRA´s Transition Study available at our website. (www.pacra.com). However, actual transition of rating may not follow the pattern observed in the past | Chapter III | 14-(f-VII)
Proprietary Information