The Pakistan Credit Rating Agency Limited

Rating Report

PakGen Power Limited

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
30-Jun-2018	AA	A1+	Stable	Maintain	-
22-Dec-2017	AA	A1+	Stable	Maintain	-
08-Jun-2017	AA	A1+	Stable	Maintain	-
31-Oct-2016	AA	A1+	Stable	Maintain	-
20-Nov-2015	AA	A1+	Negative	Maintain	-

Rating Rationale and Key Rating Drivers

The ratings reflect the regulated structure of Pakgen's business; Whereby revenues and cash flows are guaranteed by the sovereign government given adherence to agreed operational parameters. On standalone basis, increase in delta losses between required and actual efficiency levels has impacted the operational performance. Negative delta remained a drag. However, topline of the company has improved owing to increase in the price of furnace oil and rupee depreciation again dollar, which in turn translating into better profitably. Receivable days has increased significantly in 3MCY18 owing to deteriorated payment behavior from the power purchaser. The company's financial profile, though adequate, is highly dependent on the behavior of the power purchaser. The Company has been consistent in paying dividends. Pakgen Power repaid its long term project debt in 2010. However, current borrowings reflects the need to bridge the working capital requirements. Moreover, Company's profitability has increased because of reduction in delta losses.

Company was pursuing conversion of plant from oil fired to coal. However there has been no further development owing to government policy to restrict use of imported coal. Additionally, company was also considering to enter in to a solar power energy projects, which is currently on hold due to pending approval by NTDC.

Upholding operational performance in line with agreed performance levels would remain a key rating driver. Accumulation of debt to finance CAPEX - the coal conversion project and/or fresh investment in new power project – may impact financial risk profile of the company. Meanwhile, any significant increase in overdue receivables, as a result of rising circular debt, may negatively impact the ratings.

Disclosure	
Name of Rated Entity	PakGen Power Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology | Correlation between long-term and short-term rating scale(Jun-17),Methodology | Criteria Modifiers(Jun-17),Methodology | Independent Power Producers (IPP)(May-17)
Related Research	Sector Study | Power(Apr-18)
Rating Analysts	Hamza Ghalib | hamza.ghalib@pacra.com | +92-42-35869504

Pakgen Power Limited – Profile	
Incorporated	1994
Major business lines	Independent Power Producer
Legal status	Public Limited
COD	1998
Name plate capacity	365 MW
Primary Fuel	RFO
Plant Location	Mehmood Kot, Muzaffargarh

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

- Nishat Group (40%) and City School (17%) are the major sponsors of the company.
- Major Sponsor – Nishat Group – is the biggest conglomerate of the country with interests in textile,cement, power, real estate,banking and insurance.
- The City Schools (Pvt.) Limited (CSPL) established in 1978, is today one of the largest private school networks in Pakistan with branches in all the major cities across the country.
- Listed on Pakistan Stock Exchange.

GOVERNANCE

- The board is majority controlled by NG, with a total of seven nominated members including the chairman – Mr. Hassan Mansha, while rest six members are non-executive directors.
- Board members are from different educational and professional background bringing diversified professional experience and knowledge on the board.
- The board has formed two committees Audit Committee and Human Resource & Remuneration Committee.
- Mr. Hassan Mansha - chairman of the board holds position of Group Head-Energy and directorship of six other companies.

MANAGEMENT AND CONTROL

- Mr. Ghazanfar Hussain Mirza is CEO since Aug-14 and has over three decades of experience in business development and corporate management.
- Pakgen has a lean organizational structure with a professional management team.
- Key management directly reports to chairman which compromises efficacy of the board.
- The company maintains an adequate MIS system which helps management to keep track of all O&Ms.

BUSINESS AND OPERATIONAL RISK

- Pakgen's O&M activities are handled by an in house team trained under the expertise of AES, former O&M operator. This team is involved in O&M activities since the plant's COD and hence carries significant experience.
- Company is also considering to enter in to a solar power energy projects. However, tariff determined by NEPRA for solar energy projects remains a main obstacle.
- Progress on plant's conversion from oil fired to coal have been delayed due to government policy to restrict use of imported coal on certain projects.

PERFORMANCE

- During CY17, generation of electricity remained adequate due to sufficient demand from the power purchaser (CY17: 1,532GWhr; CY16: 1,614GWhr). Topline of the company has improved owing to increase in the price of furnace oil and rupee depreciation again dollar, which in turn translating into better profitably.
- The plant's availability remained well above required level in CY17 (Required: 86%; Actual: 100%).
- Thermal efficiency remained below par despite newly carried efficiency programs (Required: 38%; Actual: 32%) which has an impact of PKR 154mln on the profitability. Net profit of the company has increased YoY basis (CY17: PKR 1,314mln, CY16: PKR 517mln).

FINANCIAL RISK

- Debt mainly comprises short-term borrowings to finance working capital requirements and maintenance projects as at CY17 (STB: 92%; LTL: 8%) and CY16 (STB: 86%; LTL: 14%).
- During CY17, free cash flows from operations (FCFO) stood at PKR ~2,911mln (CY16: PKR ~1,953mln). The increase has been seen due to improved profitability, resulting in better converges [Interest Coverage: CY17: 4.3x, CY16: 3.2x].
- Company's leveraging increased mainly due to increase in short-term borrowings (CY17: 39%, CY16: 36%)
- Payment behavior from the power purchaser has deteriorated, subsequently an increase in trade receivables, culminating in escalation of cash cycle days (3MCY18: 354days, CY17: 249, CY16: 254days)

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BALANCE SHEET	31-Mar-18	30-Dec-17	31-Mar-17	31-Dec-16	31-Dec-15
	3M	CY17	3M	CY16	CY15
Non-Current Assets	**8,350**	**8,526**	**9,241**	**9,370**	**10,019**
Investments (Others)	**-**	**-**	**1**	**1**	**1**
Current Assets	**20,655**	**18,336**	**17,444**	**15,748**	**15,529**
Inventory	1,375	1,234	1,137	1,157	1,023
Trade Receivables	15,645	14,167	13,675	11,635	10,834
Other Current Assets	2,812	2,874	2,360	2,366	3,672
Cash & Bank Balances	824	62	273	591	1
Total Assets	**29,005**	**26,862**	**26,687**	**25,119**	**25,549**
Debt					
Short-term	10,321	9,195	8,585	7,249	5,081
Long-term (Inlc. Current Maturity of long-term debt)	669	780	1,115	1,226	1,672
Other Short term liabilities (inclusive of trade payables)	2,445	1,283	1,598	1,609	3,535
Other Long term Liabilities	3	-	-	-	-
Shareholder's Equity	**15,567**	**15,604**	**15,390**	**15,034**	**15,262**
Total Liabilities & Equity	**29,005**	**26,862**	**26,687**	**25,119**	**25,549**
INCOME STATEMENT					
Turnover	**4,111**	**19,755**	**4,854**	**16,044**	**6,523**
Gross Profit	565	1,983	553	1,316	1,979
Other Income	2	191	3	4	3
Financial Charges	(175)	(679)	(151)	(604)	(321)
Net Income	**335**	**1,314**	**355**	**517**	**1,598**
Cashflow Statement					
Free Cashflow from Operations (FCFO)	689	2,911	701	1,953	2,300
Net Cash changes in Working Capital	(797)	(3,451)	(2,024)	(1,569)	(1,654)
Net Cash from Operating Activities	(248)	(1,199)	(1,469)	(190)	158
Net Cash from InvestingActivities	(5)	(84)	(73)	(200)	(2,391)
Net Cash from Financing Activities	1,015	753	1,224	980	739
Net Cash generated during the period	762	(529)	(318)	590	(1,494)
Ratio Analysis					
Performance					
Turnover Growth	-15.3%	23.1%	65.0%	146.0%	-81.3%
Gross Margin	13.7%	10.0%	11.4%	8.2%	30.3%
Net Margin	8.2%	6.7%	7.3%	3.2%	24.5%
ROE	8.6%	8.4%	9.2%	3.4%	10.5%
Coverages					
Debt Service Coverage (X) (FCFO/Gross Interest+CMLTD)	2.4	2.6	2.7	1.9	3.0
Interest Coverage (X) (FCFO/Gross Interest)	3.9	4.3	4.7	3.2	7.2
FCFO Pre-WC/Gross interest+CMLTD	2.4	2.6	2.7	1.9	3.0
Liquidity					
Short Term Borrowings Coverage (Adjusted Quick Assets/Short Term B	1.6	1.6	1.6	1.6	2.2
Net Cash Cycle (Inventory Days + Receivable Days - Payable Days)	354.7	249.5	248.1	254.7	609.8
Capital Structure (Total Debt/Total Debt+Equity)	41.4%	39.0%	38.7%	36.1%	30.7%

Rating Scale

Credit Rating Scale & Definitions

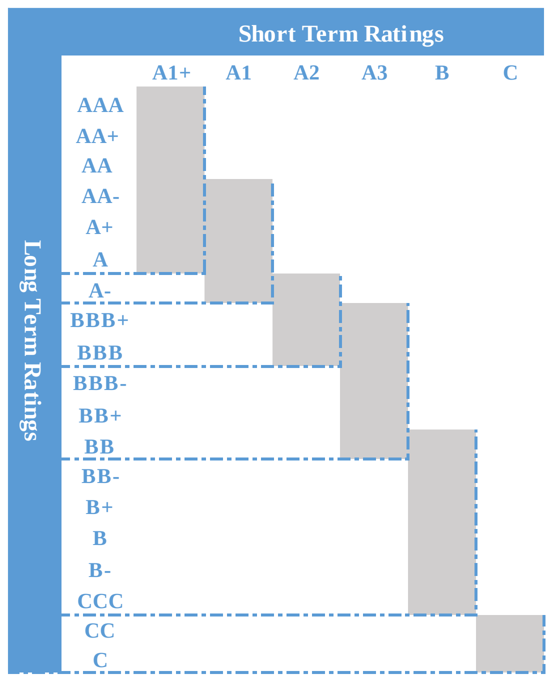
Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

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

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(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.
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(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)
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