The Pakistan Credit Rating Agency Limited

Rating Report

Motorway Operations and Rehabilitation Engineering (Private) Limited(MORE)

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
07-May-2021	AA	A1+	Stable	Maintain	-
11-May-2020	AA	A1+	Stable	Maintain	-
28-Dec-2019	AA	A1+	Stable	Upgrade	-
28-Jun-2019	AA-	A1	Positive	Maintain	-

Rating Rationale and Key Rating Drivers

Motorway Operations & Rehabilitation Engineering (Private) Limited (MORE) - a wholly owned subsidiary of Frontier Works Organization (FWO) - is specifically established for overlay and modernization of Lahore-Islamabad Motorway (M-2). The project is assigned by National Highway Authority on a Build-Operate-Transfer (BOT) basis for 20 years (beginning Apr-14). The construction phase comprised initial two years encompassing overlay and major rehabilitation work which was completed ahead of projected timeline in Aug-16. Lahore Islamabad motorway carries strategic importance as it adjoins two capitals. Over the last few operational years, MORE has witnessed consistent hike in traffic volumes and toll rates. Furthermore, rental from service areas are also providing support to profitability. The rating reflects uplift in financial profile, standalone profitability, support from rentals and investment income. Payments to NHA, as per the agreement, are being done through cash flows emanating from business. The management is staggering payments therein. The financial risk matrix has witnessed significant improvement with reduced leveraging by timely repayment of debt. Pressure of robust liquidity on the balance sheet brings additional comfort. Since traffic flow is directly linked with the revenue generation, which under Covid-19, came under stress, as the pandemic-induced slow down translated in lesser commercial traffic, thus affecting toll collection. Financial performance after the ease of lock down has depicted improvement, as economic growth picked pace. Accordingly, the cash flow coverage indicators are expected to be in comfortable zone. Going forward, the growth in traffic volumes and revenue are considered important from rating perspective.

The ratings recognize and incorporates strong financial muscle of sponsor and the explicit guarantee in place for debt repayments of MORE. Significant liquidity is lying on balance sheet, though net of relevant liabilities, is minuscule.

Disclosure	
Name of Rated Entity	Motorway Operations and Rehabilitation Engineering (Private) Limited(MORE)
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology | Corporate Ratings(Jun-20),Methodology | Correlation Between Long-Term And Short-Term Rating Scale(Jun-20),Criteria | Rating Modifier(Jun-20)
Related Research	Sector Study | Road Infrastructure(Apr-20)
Rating Analysts	Muhammad Mubashir Nazir | mubashir.nazir@pacra.com | +92-42-35869504

Profile

Legal Structure Motorway Operations and Rehabilitation Engineering (Private) Limited (MORE) was incorporated on April 11, 2014 as a Special Purpose Vehicle (SPV).

Background MORE has been established with the sole purpose of overlay and modernization of the Lahore-Islamabad Motorway (M-2).

Operations MORE signed a Concession Agreement on April 23, 2014 with National Highway Authority, an autonomous body under Ministry of Communication in Government of Pakistan, under a Build-Operate-Transfer (BOT) arrangement for a period of 20 years.

Ownership

Ownership Structure MORE is a wholly owned subsidiary of Frontier Works Organization (FWO). FWO – the parent organization – is the administrative (noncombatant) branch of Pakistan Army that comprises both military and civil personnel.

Stability MORE is an SPV established by FWO; its ownership structure will remain same over the remaining period of concession agreement.

Business Acumen The business acumen of sponsor is considered very strong given extensive past experience of construction of several projects of strategic importance.

Financial Strength The financial muscle of parent company is considered strong.

Governance

Board Structure MORE's Board of Directors consists of four FWO nominated members; three serving and one retired army officers.

Members' Profile Three board members are senior executives of FWO. The Director General FWO – Maj Gen Kamal Azfar– also designated as Chairman MORE, supervises all FWO projects. The CEO, Brig. Atif Majeed, reports to the Chairman MORE, Commander FWO.

Board Effectiveness Army officers are from engineering corp. of Pakistan Army having extensive technical expertise in field of engineering and construction. Governance framework considered adequate attributable to absence of independent member on board.

Financial Transparency M/s. EY Ford Rhodes, Chartered Accountants are appointed as the external auditor of the company. The auditors have expressed unqualified opinion on MORE's financial statements for the year ended June 30, 2019. Auditors report on the financial statments as of June 30, 2020 was not avialable.

Management

Organizational Structure MORE has a lean organizational structure. Overall operations have been divided into three main departments, a) Finance, b) Legal, and c) Business Development. The head of each department reports to the CEO.

Management Team The CEO of MORE, Brig. Atif Majeed has extensive experience in construction projects. He is supported by a team of qualified individuals. He is the key person involved in the management and operational aspects of the project. Mr. Farhan joined MORE as Chief Financial Officer after the resignation of Mr. Shaikh M. Khurshid Alam was was associated with the Company as Chief Financial Officer since Jan-17.

Effectiveness The project primarily envisages Rehabilitation and Modernization of the Lahore-Islamabad Motorway (M-2) having a total length of 357 kilometers. The starting point of the project is M-2 Thokar Niaz Baig Interchange, and the end-point is junction of M-1 & M-2 link road and National Highway (N-5).

MIS The concessionaire (MORE) has established toll plazas at the entry/exit points of M-1 and M-3 (constructed and operational). The construction of ancillary facilities under the project which includes building of restaurants/resorts, fuel stations, warehouses, and other commercial facilities are majorly completed. However, establishment of more small-scale service areas is planned.

Control Environment Modernization aspect of the project encompasses activities like landscaping and tree plantation, modernization of toll collections system, installation of state-of-the-art emergency call system, and police fine collection system, centralized operation center, and weigh-in-motion systems. Further, provision of rescue and recovery system, emergency medical response system, vehicle fitness checking system, and solar fog lighting system are also mandatory components of modernization.

Business Risk

Industry Dynamics Establishment and rehabilitation of national highways, expressways and motorways is underway since many years. During last few years, the country's road infrastructure was given special emphasis in the wake of CPEC and related projects. Eastern and Central alignment are largely completed whilst the western alignment is underway to be completed in medium to long term. After completion of whole network, traffic volume is likely to rise manifolds as time duration (time to travel) will shorten.

Relative Position M2 (Lahore - Islamabad motorway) connects two major cities of the country and has strategic importance as compare to other national highways and motorways. Currently, traffic volume includes both commercial and passenger vehicles. With the development of whole eastern and central alignment of motorways and highways in next few years, traffic volume will be impacted positively. However, as per Covid-19 implications, curtailed traffic volume is likely to be observed in next few months.

Revenues The project's revenue stream is based on i) toll collection, ii) M-2 Service Area revenues (MSA). During FY20, the revenue mix remained tilted towards toll collection 90% (FY19: toll: 90% and MSA 10%; FY18: toll: 89% and MSA 11%). Traffic volume have been witnessing an upward trend since last few years. During FY20, traffic volume followed growth trend and stayed largely the same to stand at 38.3 mln (FY19: 40 mln; FY18: ~37mln). Revenue increase is in line with last year and recorded at PKR 10.9 bln (FY19: PKR 10 bln; FY18: PKR 8.9bln) attributable to increase in both traffic volume and toll rates. The service area rentals increased to PKR 1.1 bln (FY19: PKR 1.02 bln; FY18: PKR 933mln) as service areas remained fully occupied and scheduled increase in rent.

Margins During FY20, Operating expenses stood at PKR 6.4bln (FY19: PKR 6.2bln; FY18: PKR 5.9bln) – primarily operations, maintenance cost and depreciation charge. The Company posted gross profit of PKR 4.4bln in FY20 (FY19: PKR 3.8bln; FY18: PKR 2.9bln). Administrative expenditure was increased to PKR 115mln (FY19: PKR 91mln: FY18: PKR 71mln). Other income of PKR 546mln (FY19: 291mln: FY18: PKR 91mln), supplemented the bottom-line. However, finance cost increased to PKR 3.4bln (FY19: PKR 2.9bln; FY18: PKR 2.6bln) attributable to enhanced key policy rate. Hence, the company posted net profit of PKR 1.44bln in FY20 and PKR 798mln in FY19.

Sustainability MORE, being concessionaire, established for sole purpose of overlay and modernization of M2 will operate in same capacity for the remaining years of concession agreement.

Financial Risk

Working Capital During concession period, current ratio (current assets divided by current liabilities) of at least 1:1 must be maintained by MORE. As of June 2020, MORE reported current ratio of 6.3x (FY: 19 7.8x)

Coverages As at June 20, Interest remained same 2.7x (end-Jun 19: 2.7x end-June18: 2.0x). Going forward, scheduled repayments of long term borrowing and curtailed key policy rate will positively impact coverage.

Capitalization As the project by design was debt driven, the company's debt to debt plus equity ratio stands at 70.2% atJune 20 (Jun19: 70%; Jun18: 73%). The equity base has strengthened to PKR 13.2bln as at June 20 (Jun19: 11.8bln; Jun18: PKR 10.9bln), which is a positive. Going forward, the debt repayments are as per schedule and leveraging is not expected to rise.

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ıcial Summary
PKR mln

MORE Road Infrastructure	Jun-20 12M	Jun-19 12M	Jun-18 12M
A BALANCE SHEET			
1 Non-Current Assets	28,648	32,384	36,685
2 Investments	3	87	-
3 Related Party Exposure	589	2,571	881
4 Current Assets	9,841	6,500	4,598
a Inventories	-	-	-
b Trade Receivables	*4,602*	*2,211*	*2,493*
5 Total Assets	39,080	41,542	42,164
6 Current Liabilities	1,224	1,029	586
a Trade Payables	*337*	*181*	*94*
7 Borrowings	17,872	20,991	23,858
8 Related Party Exposure	5,427	6,840	6,212
9 Non-Current Liabilities	1,327	894	517
10 Net Assets	13,230	11,789	10,991
11 Shareholders' Equity	13,230	11,789	10,991
B INCOME STATEMENT			
1 Sales	10,894	10,019	8,924
a Cost of Good Sold	*(6,493)*	*(6,206)*	*(5,925)*
2 Gross Profit	4,400	3,813	3,000
a Operating Expenses	(116)	(92)	(72)
3 Operating Profit	4,284	3,721	2,928
a Non Operating Income or (Expense)	*546*	*292*	*81*
4 Profit or (Loss) before Interest and Tax	4,830	4,013	3,009
a Total Finance Cost	*(3,389)*	*(2,874)*	*(2,605)*
b Taxation	-	*(340)*	*(188)*
6 Net Income Or (Loss)	1,441	799	216
C CASH FLOW STATEMENT			
a Free Cash Flows from Operations (FCFO)	*6,210*	*7,608*	*4,978*
b Net Cash from Operating Activities before Working Capital C	*4,073*	*6,010*	*3,284*
c Changes in Working Capital	*(391)*	*(1,471)*	*(2,420)*
1 Net Cash provided by Operating Activities	3,682	4,539	865
2 Net Cash (Used in) or Available From Investing Activities	181	(10)	(323)
3 Net Cash (Used in) or Available From Financing Activities	(3,156)	(2,319)	(1,739)
4 Net Cash generated or (Used) during the period	707	2,210	(1,197)
D RATIO ANALYSIS			
1 Performance			
a Sales Growth (for the period)	8.7%	12.3%	14.8%
b Gross Profit Margin	40.4%	38.1%	33.6%
c Net Profit Margin	13.2%	8.0%	2.4%
d Cash Conversion Efficiency (FCFO adjusted for Working Ca	53.4%	61.3%	28.7%
*e Return on Equity [Net Profit Margin * Asset Turnover * (Tot*	10.6%	6.7%	1.9%
2 Working Capital Management			
a Gross Working Capital (Average Days)	114	86	58
b Net Working Capital (Average Days)	105	81	49
c Current Ratio (Current Assets / Current Liabilities)	8.0	6.3	7.8
3 Coverages			
a EBITDA / Finance Cost	2.5	2.7	2.7
b FCFO / Finance Cost+CMLTB+Excess STB	0.9	1.3	0.9
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Fina	8.3	5.9	12.7
4 Capital Structure			
a Total Borrowings / (Total Borrowings+Shareholders' Equity)	63.8%	70.2%	73.2%
b Interest or Markup Payable (Days)	0.0	0.0	0.0
c Entity Average Borrowing Rate	13.3%	9.9%	8.3%

Credit Rating

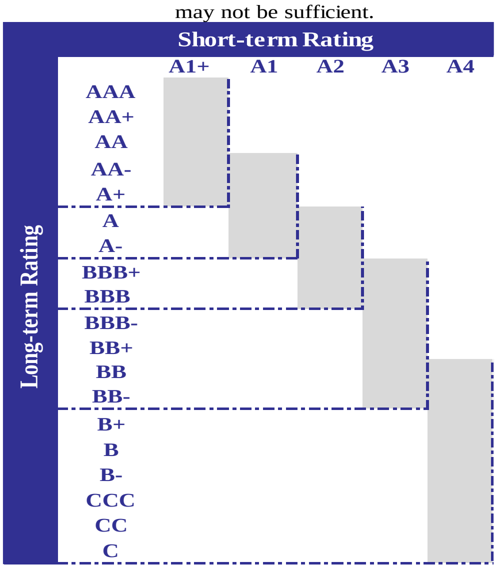
Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

Long-term Rating

Scale	Definition
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 Rating

Scale	Definition
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
A4	The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions. Liquidity may not be sufficient.



**The correlation shown is indicative and, in certain cases, may not hold.*

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 some material identifiable event with indeterminable rating implications. 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 rating 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) the debt instrument is redeemed, c) the rating remains suspended for six months, d) the entity/issuer defaults., or/and e) 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.

Surveillance. Surveillance on a publicly disseminated rating opinion is carried out on an ongoing basis till it is formally suspended or withdrawn. A comprehensive surveillance of rating opinion is carried out at least once every six months. However, a rating opinion may be reviewed in the intervening period if it is necessitated by any material happening.

Note. This scale is applicable to the following methodology(s):

Entities

a) Broker Entity Rating
b) Corporate Rating
c) Financial Institution Rating
d) Holding Company Rating
e) Independent Power Producer Rating
f) Microfinance Institution Rating
g) Non-Banking Finance Companies (NBFCs) Rating

Instruments

a) Basel III Compliant Debt Instrument Rating
b) Debt Instrument Rating
c) Sukuk Rating

Regulatory and Supplementary Disclosure
(Credit Rating Companies Regulations,2016)

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