The Pakistan Credit Rating Agency Limited

Rating Report

K-Electric | PPSTS-1 | TBI

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
28-Jan-2022	AA	A1+	Stable	Preliminary	-

Rating Rationale and Key Rating Drivers

The ratings reflect sustained performance metrics of the company. Amid COVID-19 Pandemic despite unfavorable circumstances the Company maintained stability in its turnover. During FY21, units sent out grew by 9.6%, owing to improved macroeconomic factors, along with substantial investment across the power value chain. Further, with targeted loss reduction initiatives, the Company managed to reduce its T&D losses to 17.5% from 19.7% in FY 2020. The performance levels showed further improvement in 3MFY22 when, T&D losses decreased by 3.1% while units billed increased by 3.2%, though units sent out showed a marginal decrease of 0.7%. With economic revival, the Company's performance took a notable upsurge in its performance, and reported a net profit of ~PKR 2.9bln in 3MFY22, against a profit of ~PKR 1.1bln in 3MFY21 (FY21: PKR 12bln, FY20: -PKR 3bln). Business risk profile draws support from growing demand for electricity and continuous improvement across various operational metrics. The company continued to add to its asset base: expansion was noted in plants, distribution and transmission. The Company is pursuing its 900 MW RLNG project on fast-track basis. In addition to this additional supply of 450-600 MW from National Grid has also been achieved through successful completion of rehabilitation works at KDA-Jamshoro lines.

The performance metrics in the ongoing financial year has shown similar trends with more focus on the production and sale of power units. At the same time, upholding business and financial metrics is of utmost importance.

Disclosure

Name of Rated Entity	K-Electric	PPSTS-1	TBI
Type of Relationship	Solicited
Purpose of the Rating	Debt Instrument Rating
Applicable Criteria	Methodology	Debt Instrument Rating(Jun-21),Criteria	Correlation Between Long-term & Short-term Rating Scales(Jun-21),Criteria	Rating Modifiers(Jun-21)
Related Research	Sector Study	Power(Jan-22)
Rating Analysts	Bazah Tul Qamar	bazahtul.qamar@pacra.com	+92-42-35869504

K – ELECTRIC LIMITED PROFILE	
Incorporated	1913
Major business lines	Vertically-integrated power utility
Legal status	Public Limited (Listed)
Installed Capacity	2,000 + MW as at 30th June,2021.
No. of Consumers	~3.2 Mn
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.

PROFILE & OWNERSHIP

- K-Electric Limited, a vertically-integrated power utility, has been in operations for over a century. As part of diversification strategy of KE, a wholly owned subsidiary named KE Venture Company (Pvt) Ltd (KEVCL) was incorporated on July 30, 2020 to undertake different initiatives in the energy sector. Additionally, another company, K-Solar (Pvt) Ltd which commenced its operations in June 2021 has been incorporated under KEVCL. K-Solar specializes in distributed generation business and will provide sustainable and long-term solar solutions to residential, commercial and industrial consumers.
- Total installed capacity of K-Electric Limited power generation plants is 2,000 + MW as at September 30, 2021. K-Electric Limited has an arrangement with external power producers for ~1,900 MW including 1,250 MW from the National Grids.
- The company is ~66% owned by KES Power Limited, while GoP holds ~24% stake. KES Power is the major shareholder of the Company. KES Power is a consortium of Al-Jomaih Group of KSA, NIG of Kuwait and IGCF, a private equity fund formerly managed by Abraaj comprised of several Middle East institutional investors. KES Power has entered into a Share Purchase Agreement with Shanghai Electric Power Company Limited (SEP) for sale of up to 66.4% shares of K-Electric Limited. The transaction will close once customary closing conditions and requisite regulatory approvals are obtained.

GOVERNANCE

- The company's board of directors comprises of thirteen directors. Mr. Shan A. Ashary currently is appointed as a new Chairman of the Board effective 7 September 2020. All the board members are seasoned professionals having interests in various sectors of the industry.
- There are six committees at the board level, namely i) Audit, ii) Finance, ii) Human Resource & Remuneration iv) Strategy & Projects Committee and v) Risk Management & Safety, vi) Board Regulatory Affairs Committee This ensures effective oversight of the company's affairs and strengthening the board's governance role.
- GOP has notified on 22 May 2019, Multiyear Tariff (MYT) for K-Electric Limited for the period of seven (7) years applicable from 1 July 2016 to 30 June 2023.

MANAGEMENT

- The management control of the company vests with KES Power Limited, being the largest shareholder.
- Mr. Moonis Alvi has been spearheading the company since being the CEO in June 2018. He has also previously served as the Chief Financial Officer of K-Electric Limited.
- The organizational structure of K-Electric Limited is divided into three main business areas, namely (i) Generation, (ii) Transmission, and (iii) Distribution. Meanwhile, support functions such as Treasury & Corporate Finance, Marketing, and HR, supply chain etc. are centralized at the company level and are headed by professionals having considerable experience in their respective fields.
- 111th Annual General meeting of K-Electric will be held through video conferencing on October 13, 2021.

BUSINESS AND OPERATIONAL RISK

- During FY21, with improved macroeconomic environment along with investments of around PKR 80.9 billion across the power value chain, the Company continued to show strong operational performance with an increase in units sent out by 9.6%. The performance levels showed further improvement in 3MFY22 when, T&D losses decreased by 3.1%, while units billed increased by 3.2%, though units sent out showed a marginal decrease of 0.7%.
- TP-1000 is a transmission enhancement project by K-Electric Limited of over USD 450mln which will enable the utility to enhance transmission capacity by 1000 MVs. To date more than 90% of the project has been completed - 6 grid stations and 26 power trafos have been added under the project. KE is setting up a 900 MW RLNG Project. Effective and timely execution of project is likely to further uplift company's profile in medium to long term.
- During FY21, KE has +received a TDC receipt of PKR 6billion post approval of ECC. It helped Company to continue to pay fuel suppliers and IPPs, with consideration that consumers have been offered a longer payment term in this critical time. Additionally, the finance cost reduced due to reduced borrowing rate. This coupled with improved operational improvements has helped turn around KE back into profits.

PERFORMANCE

- Units billed during 3MFY22 have increased to 4,677 GWh (3MFY21:4,531GWh). Recovery ratio has started to show improvement to 97% during 3MFY22 (FY21: 95%). Furthermore, the management is anticipating improvement in public sector recoveries on account of settlement of old recoveries from KWSB.

FINANCIAL RISK

- During 3MFY22, total receivables of the company are reported at PKR 108,598mln (FY21: PKR 104,714mln) owing to delay in public sector recoveries and the prevailing circular debt crisis in the country.
- The company has strong cash generation ability. The outstanding receivable balances and tariff differential claims have placed constraints on cash flow streams, and for working capital requirement of the company is resorting to short term debt avenues. The leverage is increasing over years yet in the comfortable range, particularly in the context of equity base. The equity base itself is strong.

ABOUT THE INSTRUMENT

- K-Electric is in the process of issuing a rated, privately placed, short term, unsecured Sukuk of PKR 4,500mln in February, 2022, to finance the company's working capital requirements. The tenor of PPSTS 1 is up to 6 months and carries a profit rate of 6 months KIBOR+85bps. Profit will be realized at the time of maturity., to finance the company's working capital requirements.

Financial Summary

The Pakistan Credit Rating Agency Limited *PKR mln*

	Sep-21	Jun-21	Jun-20	Jun-19
K Electric Limited				
Power	3M	12M	12M	12M
A BALANCE SHEET				
1 Non-Current Assets	430,151	424,484	361,321	326,857
2 Investments	2,972	2,987	3,048	-
3 Related Party Exposure	182	182	-	-
4 Current Assets	439,642	408,024	339,045	272,008
a Inventories	*3,822*	*3,024*	*647*	*12,078*
b Trade Receivables	*108,599*	*104,714*	*99,832*	*99,928*
5 Total Assets	872,947	835,677	703,414	598,865
6 Current Liabilities	413,076	382,145	295,378	215,752
a Trade Payables	*321,258*	*297,613*	*217,625*	*190,795*
7 Borrowings	187,440	184,300	155,574	129,511
8 Related Party Exposure	-	-	-	-
9 Non-Current Liabilities	45,578	45,281	41,795	39,113
10 Net Assets	226,854	223,952	210,667	214,489
11 Shareholders' Equity	226,854	223,952	210,658	214,489
B INCOME STATEMENT				
1 Sales	114,139	325,049	288,807	289,119
a Cost of Good Sold	*(97,499)*	*(265,854)*	*(244,914)*	*(238,413)*
2 Gross Profit	16,640	59,195	43,893	50,706
a Operating Expenses	(6,872)	(25,225)	(21,523)	(43,103)
3 Operating Profit	9,768	33,970	22,370	7,603
a Non Operating Income or (Expense)	*(2,778)*	*(7,511)*	*(5,275)*	*7,564*
4 Profit or (Loss) before Interest and Tax	6,989	26,459	17,096	15,167
a Total Finance Cost	*(2,988)*	*(11,113)*	*(16,737)*	*(6,285)*
b Taxation	*(1,099)*	*(3,348)*	*(3,318)*	*8,391*
6 Net Income Or (Loss)	2,902	11,998	(2,959)	17,274
C CASH FLOW STATEMENT				
a Free Cash Flows from Operations (FCFO)	*10,863*	*59,424*	*48,785*	*51,725*
b Net Cash from Operating Activities before Working Capital Changes	*8,175*	*44,556*	*27,160*	*42,190*
c Changes in Working Capital	*(1,712)*	*(2,296)*	*(4,512)*	*(59,074)*
1 Net Cash provided by Operating Activities	6,463	42,259	22,648	(16,884)
2 Net Cash (Used in) or Available From Investing Activities	(9,626)	(74,465)	(49,411)	(33,842)
3 Net Cash (Used in) or Available From Financing Activities	4,627	22,061	26,415	52,012
4 Net Cash generated or (Used) during the period	1,463	(10,144)	(349)	1,285
D RATIO ANALYSIS				
1 Performance				
a Sales Growth (for the period)	40.5%	12.5%	-0.1%	30.6%
b Gross Profit Margin	14.6%	18.2%	15.2%	17.5%
c Net Profit Margin	2.5%	3.7%	-1.0%	6.0%
d Cash Conversion Efficiency (FCFO adjusted for Working Capital/Sales)	8.0%	17.6%	15.3%	-2.5%
*e Return on Equity [Net Profit Margin * Asset Turnover * (Total Assets/Sh*	5.2%	5.5%	-1.4%	8.2%
2 Working Capital Management				
a Gross Working Capital (Average Days)	88	117	134	143
b Net Working Capital (Average Days)	-159	-172	-124	-36
c Current Ratio (Current Assets / Current Liabilities)	1.1	1.1	1.1	1.3
3 Coverages				
a EBITDA / Finance Cost	4.3	6.6	3.7	7.8
b FCFO / Finance Cost+CMLTB+Excess STB	0.4	0.6	0.9	1.7
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)	5.1	3.1	3.2	1.6
4 Capital Structure				
a Total Borrowings / (Total Borrowings+Shareholders' Equity)	45.2%	45.1%	42.5%	37.6%
b Interest or Markup Payable (Days)	273.7	360.1	228.8	437.2
c Entity Average Borrowing Rate	6.8%	5.3%	9.3%	6.2%

Credit Rating

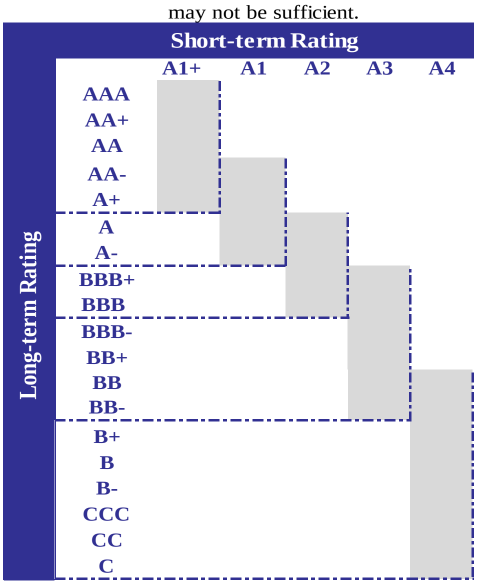
Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

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):

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

Regulatory and Supplementary Disclosure

Nature of Instrument	Size of Issue (PKR)	Tenor	Security	Quantum of Security	Nature of Assets	Trustee	Book Value of Assets (PKR mln)
Rated, Privately Placed, Short Term Sukuk (PPSTS-1)	4,500mln	6 months	Unsecured	N/A	N/A	Meezan Bank Limited	N/A

Name of Issuer	K- Electric Limited (K-Electric)
Issue Date	2-Feb-22
Maturity	2-Aug-22
Option	N/A

Due Date Principal*	Opening Principal	Principal Repayment*	Due Date Markup/ Profit*	Markup/Profit rate	6M Kibor Plus 85bps	Markup/Profit Payment	Installment Payable	Principal Outstanding
	PKR in mln					PKR in mln		
Issuance								4,500
2-Feb-22	4,500			6M KIBOR + 0.85%	11.68%		-	4,500
2-Aug-22	4,500	4,500	2-Aug-22	6M KIBOR + 0.85%	11.68%	263	4,237	-
		4,500				**263**	**4,237**	