The Pakistan Credit Rating Agency Limited

Rating Report

Kohinoor Energy Limited

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
27-Sep-2019	AA	A1+	Stable	Maintain	-
28-Mar-2019	AA	A1+	Stable	Maintain	-
27-Dec-2018	AA	A1+	Stable	Maintain	-
30-Jun-2018	AA	A1+	Stable	Maintain	-
22-Dec-2017	AA	A1+	Stable	Maintain	-
23-Jun-2017	AA	A1+	Stable	Maintain	-
31-Oct-2016	AA	A1+	Stable	Maintain	-
20-Nov-2015	AA	A1+	Stable	Maintain	-
25-Nov-2014	AA	A1+	Stable	Maintain	-
31-Oct-2013	AA	A1+	Stable	Maintain	-

Rating Rationale and Key Rating Drivers

The ratings of Kohinoor Energy Limited (Kohinoor Energy) reflect its stable business profile emanating from a secured regulatory structure. This entails sovereign guaranteed revenues and cash flows, given adherence to agreed performance benchmarks. Kohinoor Energy continues to meet its availability (86.07%) and efficiency (43.5%) benchmarks - an outcome of technically sound O&M team, robust systems and controls, and strong governance structure. Nevertheless, delayed payments from the power purchaser remained a challenge. Business risk is considered low exhibited by demand risk coverage under the Power Purchase Agreement signed between WAPDA and the company. Current borrowings mainly short-term reflects the need to meet the working capital requirements and maintenance projects. Short-term borrowing lines are available and mainly used to fund any shortfall in working capital requirement. There is cushion available in short term lines. Given the liquidity situation, utilization is imputed to go up. Settlement of overdue receivables is crucial. Meanwhile, the company continues to enjoy sound coverages, though its financial profile is highly dependent on the timely repayment of the receivables. The Company has been paying dividends which in times of need is an internal source of liquidity available. The ratings continue to take comfort from Kohinoor Energy's association with good business groups - Toyota Tsusho Corporation and Saigol Group.

Although well-managed, in-house O&M activities expose the company to operational risk; thus upholding strong operational performance in line with agreed performance levels would remain a key driver of the ratings. Meanwhile, any significant accumulation in receivables, thereby impacting the financial profile of the company may have negative effects.

Disclosure	
Name of Rated Entity	Kohinoor Energy Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	PACRA_Methodology_IPP_FY19(Jun-19),PACRA_Crtieria_LT ST Relationship_FY19(Jun-19),PACRA_Criteria_Rating Modifiers_FY19(Jun-19)
Related Research	Sector Study | Power(Jan-19)
Rating Analysts	Mubasher Bhatti | mubasher.bhatti@pacra.com | +92-42-35869504

Profile

Plant The power plant comprises eight Residual Fuel Oil fired diesel generators have a capacity of 15.68 MW each along with a combined heat cycle recovery system providing an additional output of 6MW through a steam turbine. While using RFO as the primary fuel, the plant also has the capacity to use light fuel oil (LFO) for startup. Net rated capacity, after accounting for auxiliary consumption, is 124MW.

Tariff Company's key source of earnings is the generation tariff from the power purchaser, WAPDA. The reference generation tariff comprises a capacity charge component and an energy charge component. The former is based upon dependable capacity and constitutes a minimum tariff guaranteed to the company which covers the fixed O&M costs, insurance charges, working capital funding costs and return on equity. The levelized tariff for the period of 30 years is US cents/kWh 5.2492.

Return On Project The components of Capacity Payments are being indexed with the variation in US Dollar Exchange rate and US CPI to ensure the dollar-based return on investment.

Ownership

Ownership Structure The company has a diversified shareholding pattern - majority held by Toyota Tsusho Group (36%) followed by Saigol family (26%). Meanwhile, National Bank of Pakistan (NBP) holds 6% and Wartsila Pakistan a meager 2%. The remaining shareholding is held by financial institutions, joint stock companies, and individuals.

Stability Stability in the IPPs is drawn from the agreements signed between the company and power purchaser. Stability factor is considered strong.

Business Acumen Toyota Tsusho Corporation (TTC) is one of the largest trading corporations in the world. In addition to automobiles, the company deals in metals, chemicals, electronics, machinery & energy globally. Tomen Power Singapore, the subsidiary of TTC is in the business of operating and managing wind-based power projects. PEL, the flagship company of the Saigol group, is mainly engaged in the manufacturing and sale of electrical equipment and home appliances. However, despite the diversification, the group has a strong financial profile and proven business acumen.

Financial Strength Company’s sponsors have the ability and showed the willingness to support the entity both on a continuing basis, and support in times of crisis. Additionally, the financial strength of the sponsors is considered strong as the sponsors have well diversified profitable businesses.

Governance

Board Structure BoD comprises seven members including the Chief Executive Officer. The board members are professionals with experience in managing the business affairs of companies in different sectors. The board includes four representatives of TTC, two representatives of the Saigol group and one representative of Wartsila Pakistan.

Members’ Profile The chairman, Mr. Naseem Saigol, is nominated by the Saigol Group. He is a renowned businessman and also chairs the Board of Saigol Group. The board has been actively involved in providing strategic guidance to the company and implementing strong internal control framework.

Board Effectiveness The board has made two committees namely the Audit Committee and Human Resource & Remuneration Committee which ensures effective governance of the company. The directors of the company have attended directors training programs as per the mandatory requirement of SECP to ensure that they are aware of their duties and responsibilities and can effectively manage the affairs of listed companies on behalf of the shareholders.

Financial Transparency A.F. Ferguson & Co. Chartered Accountants are the external auditors of the company. They expressed an unqualified opinion on the company’s accounts as at 30 June 2018.

Management

Organizational Structure The management's role in an IPP is confined largely to financial matters and regulatory interaction. In light of this, KEL has a lean organizational structure. The organizational structure of the company is divided into two major functional areas (i) Technical and (ii) Support functions.

Management Team Mr. Sheikh M. Shakeel is the CEO of the company. He carries work experience of over thirty years. Mr. Shakeel is assisted by a team of qualified individuals with significant experience in the energy business. He is supported by a team of qualified people.

Effectiveness Over the years Company’s effective management played a significant role in empowering the organization through its progressive results. Additionally, management’s effective decision-making cause processes more systematic while robustness of control systems is considered a reflection of strong management, which is considered positive.

Control Environment The company takes advantage of advanced I.T. solutions to deliver comparatively better on many fronts. Moreover, KEL's quality of the I.T. infrastructure and the breadth and depth of activities performed has remained well satisfactory.

Operational Risk

Power Purchase Agreement According to the agreement, the obligations of the power purchaser are guaranteed by the Government of Pakistan. Furthermore, a stable revenue stream is also ensured through the minimum guaranteed capacity charge (the component of the tariff received irrespective of electricity production).

Operation And Maintenance Previously O&M activities were handled in-house while major maintenance work was managed by Wartsila Pakistan. Since 2016, the company started to undertake major O&M in-house that has produced a meaningful outcome. As a result of this, the Company has successfully demonstrated 129.78 MW capacity during the Annual Dependable Capacity test conducted by WAPDA on 3 May 2019.

Resource Risk Fuel supply risk terminates at the fuel supplier - PSO who will be responsible for payment of damages to the company resulting from its failure to deliver fuel as per the Fuel Supply Agreement.

Insurance Cover The company has adequate insurance coverage for property damage and business interruption.

Performance Risk

Industry Dynamics Pakistan total power generation is increasing on the back of new power projects under CPEC. Owing to newly installed plants, Pakistan’s energy mix is shifting towards Solar/Gas/RLNG and coal from Furnace Oil and other expensive sources. Pakistan total power generation is increasing on the back of new power projects under CPEC. During July - March FY2019, installed capacity of electricity reached 34,282 MW, which was 33,433 MW in corresponding period last year, thus, posting a growth of 2.5 percent. Although electricity generation varies due to availability of inputs and other constraints, the generation increased from 82,011 GWh to 84,680 GWh, posting a growth of 2.1 percent during the period under discussion.

Generation During 9MY19 electricity of 315.776 GWh was produced (FY18: 645.395 GWhr, FY17: 864.649 GWhr) at an average thermal efficiency of 44.56%. This decline is seen owing to less demand for electricity by power purchaser owing to changing energy mix.

Performance Benchmark Company’s availability remained satisfactory (Required: 86.07%, Actual: ~92%).

Financial Risk

Financing Structure Analysis The company has repaid its long-term project debt in 2008.

Liquidity Profile At 31 March 2019, total receivables of the company stood at ~PKR 6.5bln (FY18:~PKR 6.6bln, FY17: ~PKR 4.9bln), an decrease of ~1.5%. Circular debt continues to be an issue for companies operating in the power sector. Consequently, IPPs have to manage their liquidity requirements through short-term borrowings.

Working Capital Financing At 31 March 2019, total available working capital lines are ~PKR 7.4bln of which ~60% has been utilized. Resultantly, remaining cushion in the available working capital facilities is ~40% currently. Cash cycle has remained stable (9MFY19: 309days, FY18: 309days, FY17: 227 days).

Cash Flow Analysis During 9MFY19, free cash flows from operations (FCFO) stood at PKR 1,246mln (FY18: PKR 1,471mln, FY17: PKR 1,321mln). Coverages have been declining owing to higher interest cost during the period under review [Interest coverage: 9MFY19: 3.5x, FY18: 5.5x, FY17: 7.4x].

Capitalization The Company has a moderately leveraged capital structure that has increased on the back of an increase in short-term borrowings (D/D+E: 9MFY19: 42%, FY18: 47%, FY17: 37%). Debt comprises short-term borrowings to finance working capital requirements.

Kohinoor Energy Limited

BALANCE SHEET	31-Mar-19	30-Jun-18	30-Jun-17	30-Jun-16
	9M	FY18	FY17	FY16
Non-Current Assets	**3,645**	**3,504**	**3,681**	**3,909**
Investments (Others)	-	-	-	-
Current Assets	**7,360**	**8,022**	**6,194**	**4,880**
Inventory	564	687	579	539
Trade Receivables	6,548	6,645	4,910	3,607
Other Current Assets	165	535	561	700
Cash & Bank Balances	83	155	145	34
Total Assets	**11,005**	**11,526**	**9,875**	**8,789**
Debt				
Short-term	4,447	5,286	3,579	2,474
Long-term (Inlc. Current Maturity of long-term debt)	-	-	-	**30**
Other Short term liabilities (inclusive of trade payables)	379	235	240	193
Other Long term Liabilities	-	-	-	-
Shareholder's Equity	**6,179**	**6,005**	**6,057**	**6,092**
Total Liabilities & Equity	**11,005**	**11,526**	**9,875**	**8,789**
INCOME STATEMENT				
Turnover	**5,897**	**8,283**	**8,224**	**7,284**
Gross Profit	1,160	1,263	1,236	1,109
Other Income	1	1	0	0
Financial Charges	(358)	(268)	(178)	(140)
Net Income	**597**	**730**	**805**	**696**
Cashflow Statement				
Free Cashflow from Operations (FCFO)	1,246	1,471	1,321	1,183
Net Cash changes in Working Capital	655	(1,956)	(1,166)	(202)
Net Cash from Operating Activities	1,608	(736)	(5)	843
Net Cash from InvestingActivities	(437)	(195)	(110)	(121)
Net Cash from Financing Activities	(1,242)	941	226	(831)
Net Cash generated during the period	(72)	10	111	(109)
Ratio Analysis				
Performance				
Turnover Growth	4.0%	0.7%	12.9%	-37.5%
Gross Margin	19.7%	15.2%	15.0%	15.2%
Net Margin	10.1%	8.8%	9.8%	9.5%
ROE	12.9%	12.2%	13.3%	11.4%
Coverages				
Debt Service Coverage (X) (FCFO/Gross Interest+CMLTD)	3.5	5.5	7.4	6.9
Interest Coverage (X) (FCFO/Gross Interest)	3.5	5.5	7.4	8.4
FCFO Pre-WC/Gross interest+CMLTD	3.5	5.5	7.4	6.9
Liquidity				
Short Term Borrowings Coverage (Adjusted Quick Assets/Short Te	1.5	1.3	1.4	1.5
Net Cash Cycle (Inventory Days + Receivable Days - Payable Days	308.6	308.9	227.6	187.8
Capital Structure (Total Debt/Total Debt+Equity)	41.8%	46.8%	37.1%	29.1%

Rating Scale | Corporate

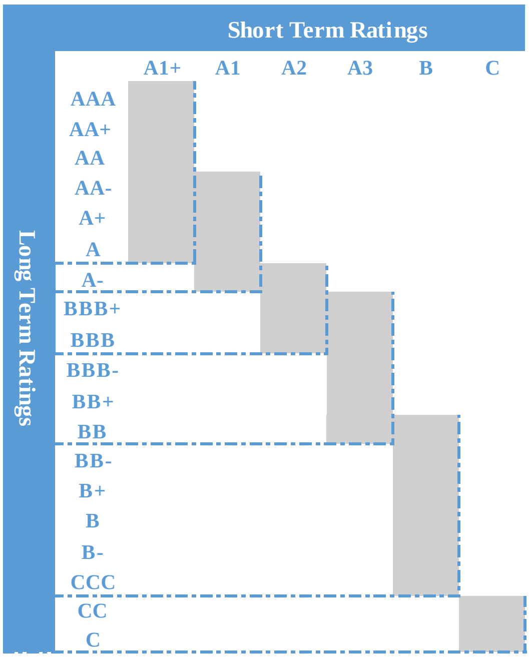
2019

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.

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