RATING REPORT

K-Electric Limited

REPORT DATE:
February 27, 2019

RATING ANALYSTS:
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RATING DETAILS

Rating Category	Latest Rating		Previous Rating	
	Long-term	Short-term	Long-term	Short-term
Entity	AA	A-1	AA	A-1
Sukuk – 3 (Rs. 1.5b)	AA	-	AA	-
Sukuk – 4 (Rs. 22b)	AA+	-	AA+	-
Rating Outlook	Rating Watch-Developing *February 25, 2019*		Rating Watch-Developing *March 07, 2018*	
ICP-2	-	A-1 *February 25, 2019*	-	

COMPANY INFORMATION

Incorporated in 1913	**External auditors:** M/s. A.F. Ferguson & Co, Chartered Accountants and M/s. BDO Ebrahim & Co, Chartered Accountants
Public Limited Company	**Chief Executive Officer:** Syed Moonis Abdullah Alvi
Key Shareholders (with stake 5% or more):	**Chairman:** Mr. Ikram Sehgal
KES Power Limited – 66.40%	
Government of Pakistan – 24.36%	

APPLICABLE METHODOLOGY(IES)

JCR-VIS Entity Rating Criteria : ***Industrial Corporates (October 2003)***
http://www.vis.com.pk/images/IndustrialCorp.pdf

Rating The Issue (September 2014)
http://vis.com.pk/Images/criteria_instrument.pdf

K-Electric Limited

OVERVIEW OF THE INSTITUTION

K-Electric Limited (KE) was incorporated as a limited liability company in 1913. It is a vertically integrated utility responsible for generation, transmission and distribution of electricity in Karachi. Abraaj Capital, through KES Power, is the major shareholder of the company.

Profile of Chairman

With more than 40 years of business experience, Ikram Sehgal is Chairman Pathfinder Group Pakistan, employing several thousand people in 50 towns and cities across Pakistan. Ikram Sehgal has served on many Boards, including Bank Alfalah for 16 years

Profile of CEO

Mr. Moonis Alvi was appointed CEO of K-Electric in June'2018. Mr. Alvi has more than 28 years of diversified experience in the finance industry, with a focus towards driving operational efficiencies, financial planning and capital restructuring

RATING RATIONALE

K-Electric Limited (KE) is a vertically integrated utility responsible for generation, transmission and distribution of electricity in Karachi. Abraaj Capital, through KES Power, is the major shareholder of the company. Shanghai Electric Power (SEP) intends to acquire up to 66.4% stake in KEL subject to receipt of requisite regulatory and other approvals. Initially, SEP had bid the acquisition of 66.4% shareholding at USD 1.77b (Rs. 194.7b) at approximated Rs. 10.6/share. KE has received fresh public announcement of intention to acquire 66.4% stake from SEP on 24th December 2018. The Company has appointed external auditors (M/s. A.F. Ferguson & Co, Chartered Accountants and M/s. BDO Ebrahim & Co, Chartered Accountants have been appointed as joint auditors) who are in the process of completing the audit. Annual General Meeting is planned to be convened once audited financial statements are available.

The assigned ratings predicate the strategic importance of KE as a vertically integrated utility having exclusive rights to distribute electricity in the largest metropolitan city of Pakistan. Business risk profile draws support from growing demand for electricity continuous improvement across various operational metrics including further reduction in transmission & distribution losses.

	Rs. KWh
Previous Tariff	**15.60**
Tariff sought by KE in Review Petition	**16.10**
Revised Tariff (Mar'17)	**12.07**
Revised Tariff – After Review Petition (Oct'2017)	**12.77**
Revised Tariff – After Reconsideration request (July'2018)	**12.82**

Financial risk profile post announcement of the new tariff is expected to remain sound. NEPRA has determined tariff of Rs. 12.8172 per Kwh for the period commencing from July 1st, 2016 to June 30th, 2023. The new Multi-Year Tariff comprises of three segments i.e. Generation, Transmission and Distribution where tariffs for the three segments were determined at Rs. 9.7351 per Kwh, Rs. 0.6192 per Kwh and Rs. 1.3890 per Kwh, respectively. The tariff is being contested by KE.

Debt levels of the Company have witnessed an increasing trend over the last one year and are projected to continue to grow as the Company forges ahead with its investment plans. Major ongoing investments include 900 MW BQPS-III project and TP-1000 project (Transmission Enhancement Plan of US$ 450m). Resultantly, with increase in debt levels, cash flow coverage of the outstanding debt has declined but is expected to improve once increase in cash flows materializes. Even at the revised tariff and incorporating select adjustments, VIS expects debt servicing to remain adequate over the rating horizon.

The assigned ratings to Sukuk issued by KE incorporate adequate debt servicing capacity and structure of the Sukuk. The entire Sukuk issue has repayment linked to specific receivables from 495 identified industrial customers, which have an extended history of timely payments with the Company and have priority of electricity supply over other consumers. Over the last one year (Nov'2017 to October'2018), recovery ratio from these customers has stood at around 99%. Other structural features of the Sukuk include retention of amount equivalent to one-third of the quarterly installment by the collection agent from the revenues of these 495 customers to meet the upcoming installment while excess proceeds after meeting the retention requirement is being released to KE each month.

K-Electric Limited — Appendix I

FINANCIAL SUMMARY *(amounts in PKR billions)*

BALANCE SHEET	**FY16**	**FY15**	**FY14**
Fixed Assets	223.5	214.0	173.1
Investments	-	-	-
Stock-in-Trade	7.9	6.8	6.0
Trade Debts	93.2	83.3	75.7
Cash & Bank Balances	2.2	1.3	0.7
Total Assets	341.9	352.9	306.3
Trade and Other Payables	81.3	105.8	106.5
Long Term Debt *(*incl. current maturity)*	32.0	31.1	28.2
Short Term Debt	23.4	36.7	44.9
Total Equity *(*excluding surplus)*	110.9	74.1	43.5
Total Equity *(*including surplus)*	160.9	128.2	71.0
INCOME STATEMENT	**FY16**	**FY15**	**FY14**
Net Sales	189.6	190.4	194.5
Gross Profit	58.2	43.3	32.2
Operating Profit	30.9	24.8	20.9
Profit After Tax	32.8	28.3	12.9
RATIO ANALYSIS	**FY16**	**FY15**	**FY14**
Gross Margin (%)	30.7	22.7	16.6
Net Working Capital	(2.1)	(19.6)	(41.8)
FFO to Total Debt (x)	96.7	51.4	35.8
FFO to Long Term Debt (x)	167.2	95.9	78.6
Debt Servicing Coverage Ratio (x)	6.9	2.3	1.7
ROAA (%)	9.2	8.8	4.4
ROAE (%)	35.4	31.8	21.5

KEY OPERATIONAL METRICS

	FY16	**FY15**	**FY14**
Transmission & Distribution Losses (%)	22.2	23.7	25.3
Fleet Efficiency (%)	37.4	37.0	37.0
Recovery Ratio (%)	90.0	90.4	87.1

ISSUE/ISSUER RATING SCALE & DEFINITIONS — Appendix II

Medium to Long-Term

AAA
Highest credit quality; the risk factors are negligible, being only slightly more than for risk-free Government of Pakistan's debt.

AA+, AA, AA-
High credit quality; Protection factors are strong. Risk is modest but may vary slightly from time to time because of economic conditions.

A+, A, A-
Good credit quality; Protection factors are adequate. Risk factors may vary with possible changes in the economy.

BBB+, BBB, BBB-
Adequate credit quality; Protection factors are reasonable and sufficient. Risk factors are considered variable if changes occur in the economy.

BB+, BB, BB-
Obligations deemed likely to be met. Protection factors are capable of weakening if changes occur in the economy. Overall quality may move up or down frequently within this category.

B+, B, B-
Obligations deemed less likely to be met. Protection factors are capable of fluctuating widely if changes occur in the economy. Overall quality may move up or down frequently within this category or into higher or lower rating grade.

CCC
Considerable uncertainty exists towards meeting the obligations. Protection factors are scarce and risk may be substantial.

CC
A high default risk

C
A very high default risk

D
Defaulted obligations

Short-Term

A-1+
Highest certainty of timely payment; Short-term liquidity, including internal operating factors and /or access to alternative sources of funds, is outstanding and safety is just below risk free Government of Pakistan's short-term obligations.

A-1
High certainty of timely payment; Liquidity factors are excellent and supported by good fundamental protection factors. Risk factors are minor.

A-2
Good certainty of timely payment. Liquidity factors and company fundamentals are sound. Access to capital markets is good. Risk factors are small.

A-3
Satisfactory liquidity and other protection factors qualify entities / issues as to investment grade. Risk factors are larger and subject to more variation. Nevertheless, timely payment is expected.

B
Speculative investment characteristics; Liquidity may not be sufficient to ensure timely payment of obligations.

C
Capacity for timely payment of obligations is doubtful.

Rating Watch: JCR-VIS places entities and issues on 'Rating Watch' when it deems that there are conditions present that necessitate re-evaluation of the assigned rating(s). Refer to our 'Criteria for Rating Watch' for details. www.jcrvis.com.pk/images/criteria_watch.pdf

Rating Outlooks: The three outlooks 'Positive', 'Stable' and 'Negative' qualify the potential direction of the assigned rating(s). An outlook is not necessarily a precursor of a rating change. Refer to our 'Criteria for Rating Outlook' for details.www.jcrvis.com.pk/images/criteria_outlook.pdf

(SO) Rating: A suffix (SO) is added to the ratings of 'structured' securities where the servicing of debt and related obligations is backed by some sort of financial assets and/or credit support from a third party to the transaction. The suffix (SO), abbreviated for 'structured obligation', denotes that the rating has been achieved on grounds of the structure backing the transaction that enhanced the credit quality of the securities and not on the basis of the credit quality of the issuing entity alone.

(blr) Rating: A suffix (blr) is added to the ratings of a particular banking facility obtained by the borrower from a financial institution. The suffix (blr), abbreviated for 'bank loan rating' denotes that the rating is based on the credit quality of the entity and security structure of the facility.

'p' Rating: A 'p' rating is assigned to entities, where the management has not requested a rating, however, agrees to provide informational support. A 'p' rating is shown with a 'p' subscript and is publicly disclosed. It is not modified by a plus (+) or a minus (-) sign which indicates relative standing within a rating category. Outlook is not assigned to these ratings. Refer to our 'Policy for Private Ratings' for details. www.jcrvis.com.pk/images/policy_ratings.pdf

'SD' Rating: An 'SD' rating is assigned when JCR-VIS believes that the ratee has selectively defaulted on a specific issue or obligation but it will continue to meet its payment obligations on other issues or obligations in a timely manner.

REGULATORY DISCLOSURE	**Appendix III**
Name of Rated Entity	K-Electric Limited
Sector	Power
Type of Relationship	Solicited
Purpose of Rating	Entity and Sukuk Ratings
Rating History	

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
		RATING TYPE: ENTITY		
20-Feb-2019	AA	A-1	Rating Watch - Developing	Reaffirmed
03-Mar-2018	AA	A-1	Rating Watch - Developing	Rating Watch - Developing
30-Dec-15	AA	A-1	Stable	Reaffirmed
1-Dec-14	AA	A-1	Stable	Upgrade
2-Jan-14	A+	A-2	Positive	Reaffirmed
25-Nov-13	A+	A-2	Positive	Initial

Rating Date	Medium to Long Term	Rating Outlook	Rating Action
	RATING TYPE: SUKUK-4		
20-Feb-2019	AA+	Rating Watch - Developing	Reaffirmed
03-Mar-2018	AA+	Rating Watch - Developing	Rating Watch - Developing
30-Dec-15	AA+	Stable	Reaffirmed
26-Mar-15	AA+	Stable	Final
29-Jan-15	AA+	Stable	Preliminary

Instrument Structure	**Sukuk 3**: Sukuk was issued in FY14 and is based on Shirkat-ul-Milk structure. Funds raised from Sukuk 3 were equivalent to Rs. 1.5b. Tenor of Sukuk-3 was 5 years respectively. **Sukuk 4:** Sukuk 4 was issued by KE in FY15 and funds raised from this Sukuk amounted to Rs. 22b. It possesses a tenor of 7 years, with a grace period of 2 years. It is structured as a diminishing musharaka arrangement and carries an interest rate of 3 month KIBOR plus 1%.
Statement by the Rating Team	VIS, the analysts involved in the rating process and members of its rating committee do not have any conflict of interest relating to the credit rating(s) mentioned herein. This rating is an opinion on credit quality only and is not a recommendation to buy or sell any securities.
Probability of Default	VIS ratings opinions express ordinal ranking of risk, from strongest to weakest, within a universe of credit risk. Ratings are not intended as

	guarantees of credit quality or as exact measures of the probability that a particular issuer or particular debt issue will default.
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