

## RATING REPORT

### K-Electric Limited – Short Term Sukuk-21

**REPORT DATE:**

November 06, 2023

**RATING ANALYSTS:**

Husnain Ali

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| RATING DETAILS                   | Final        | Preliminary  |
|----------------------------------|--------------|--------------|
|                                  | Short-Term   | Short-Term   |
| K-Electric Limited – STS-21 (5b) | A-1+         | A-1+         |
| Rating Date (STS-21)             | Nov 06, 2023 | Oct 20, 2023 |
| Rating Action                    | Final        | Preliminary  |

#### COMPANY INFORMATION

|  |   |
|--|---|
| <b>Incorporated in 1913</b>                      | <b>External auditors:</b> M/S. A.F. Ferguson & Co, Chartered Accountants. |
| <b>Public Limited Company</b>                    | <b>Chairman:</b> Mr. Mark Gerald Skelton                                  |
| <b>Key Shareholders (with stake 5% or more):</b> | <b>Chief Executive Officer:</b> Syed Moonis Abdullah Alvi                 |
| KES Power Limited – 66.4%                        |   |
| Government of Pakistan – 24.4%                   |   |

#### APPLICABLE METHODOLOGY

Applicable Rating Criteria: Industrial Corporate (May 2023)

<https://docs.vis.com.pk/docs/CorporateMethodology.pdf>

Rating The Issue (August 2023)

<https://docs.vis.com.pk/docs/Rating-the-Issue-Aug-2023.pdf>

VIS Rating Scale

<https://docs.vis.com.pk/docs/VISRatingScales.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 power utility responsible for generation, transmission and distribution of electricity in Karachi and its adjoining areas.

KES Power is the major shareholder of the Company.

**Profile of Chairman**

Mark Skelton is a Managing Director with Alvarez & Marsal's (A&M) Advisory practice in London. He brings more than 20 years of experience in corporate finance and advisory. His primary areas of concentration are cross boarder assignments, many of which involve complex stakeholder groups crossing different legal jurisdictions and waterfall classes. Mr Skelton has undertaken senior roles on numerous major UK, US, European, Emerging Markets, and Australian projects across a range of industries, including energy, power, industrials, mining, financial services, automotive, retail, property and telecommunications. Prior to joining A&M, Mr. Skelton's held senior positions in a leading independent restructuring advisory and a Big 4 firm. Mr. Skelton is a member of the Institute of Chartered Accountants in Australia and New Zealand (CAANZ)

**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. Mr. Alvi joined K-Electric in 2008 and has served as K-Electric's Chief Financial Officer and other key positions and has played an integral role in the transformation of K-Electric. He is a Fellow member of the Institute of Chartered Accountants of Pakistan.

**RATING RATIONALE**

K-Electric Limited (KE) is a vertically integrated power utility responsible for generation, transmission and distribution of electricity in Karachi and its adjoining areas including Dhabeji and Gharo in Sindh and Hub, Uthal, Vindar and Bela in Balochistan. KES Power Limited (KESP) is the major shareholder and holding company of KE. KESP is a consortium comprising Al-Jomaih Group of KSA, National Industries Group of Kuwait and IGC SPV 21, a special purpose vehicle company indirectly owned by Infrastructure and Growth Capital Fund - a private equity fund of several investors.

**Short Term Sukuk Issuance:**

- KE has raised a rated, unsecured, privately placed Short-term Sukuk (STS-21) amounting up to Rs. 5b (inclusive of green shoe option of Rs. 1b) to finance working capital requirements of the company on October 24, 2023.
- Tenor of the instrument is up to 6 months from the date of drawdown and will be redeemed in bullet at the expiry of tenor.
- Indicative rate on the instrument would be 3M KIBOR + 50 bps per annum.
- Upon review of executed legal documents and issuance of the instrument, rating has been finalized.

**Financial Risk Profile:**

- Rising socio-political instability, and macroeconomic challenges, including policy rate hike have negatively impacted the revenues and profitability of the Company during FY23. The units sent-out dropped by 7.3% due to overall economic slowdown in FY23. The Company's cash flows and coverages have been adversely impacted in FY23.
- All time high inflation has considerably impacted the consumer's ability to pay which is reflected in sizeable increase in impairment loss booked during FY23.
- Accumulated receivables from Government, continued to strain the working capital of the Company. Increase in fuel prices and non-provision of local gas supply to KE have led to augmentation in Tariff Differential Subsidy (TDS) claims receivables from GoP. Further, increase in effective borrowing rate and higher levels of borrowing due to non-payment from Government entities resulted in net loss for the Company in FY23.
- The Company is focusing on improvements on operational fronts to curtail losses. In addition, the Company remains in continuous engagement with NEPRA to expedite the determination of pending quarterly tariff variations.
- KE was awarded an integrated MYT by NEPRA for a control period of 7 years that expired in June 2023. Keeping in view learnings of the MYT 2017-2023 and the ongoing changes in power sector including Distribution (network) and Supply business being separate licensed activities, implementation of Competitive Trading Bilateral Contract Market (CTBCM) model, and the proposed countrywide central economic dispatch, KE is endeavoring for separate tariff determination for each business segment for the period post June 2023.
- Under the proposed Tariff for the next period i.e., FY24 onwards, KE has proposed indexation mechanism to account for changes in the macroeconomic factors including exchange rate, CPI, KIBOR, LIBOR etc. Accordingly, cost of debt in the proposed tariff will reflect quarterly indexation of KIBOR / LIBOR or SOFR based on actual. Further, KE has requested annual revision in investments due to changes in exchange rate and CPI. With respect to recovery loss, KE has requested recovery loss allowance based on a proposed improvement trajectory. It is to be noted that the proposed structure and salient points under new MYT are in line with existing industry practices and current tariff structure offered to IPPs, therefore, the company expects that their requests bar minor adjustments will be accepted by NEPRA after their due process.
- Amidst uncertain socio-political and macro-economic factors, managing liquidity remained a challenge. However, the Company has managed its cashflow requirements through optimization of working capital and continuous support from banks, capital markets and other financial institutions. Leverage indicators increased considerably during the reporting period. Going forward, additional

loan would be required to fund planned investments in transmission and distribution, being undertaken over the next control period from FY24 to FY30, valued at around Rs. 484b.

**Company Updates:**

- With regards to the latest quarterly tariff adjustment for K-Electric consumers, NEPRA has approved the adjustment till December 2022. NEPRA has conducted a hearing in respect of quarter ending March 2023 in May 2023 whereas hearing in respect of quarter ending June 2023 hearing is yet to be conducted. The Company remains in continuous engagement with NEPRA to expedite the determination of pending quarterly tariff variations.
- K-Electric has filed separate tariff petitions for each of its business segments including Generation, Transmission & Distribution for the period FY24-30. KE's Tariff petition for Generation Segment has been admitted by NEPRA and currently proceedings are in an advanced stage regarding approval of the same. For the Transmission and Distribution tariff petition, KE has submitted an investment plan of Rs. 484b, and the proceedings for these are currently in their final stages. The approval for the investment plan which will be followed by Tariff petition for Transmission and Distribution business is expected to be completed in next couple of months.
- The overall control of the Company vests in Board of Directors (BoD) which comprises of thirteen members including the CEO. The majority on the Board is controlled by KES Power Ltd. where Mr. Mark Gerard Skelton has been appointed by the BOD as Chairman. In October 2022, Mr. Boudewijn Clemens Wentink, Ch. Khaqan Saadullah Khan and Ms. Sadia Khurram resigned from the position of Non-Executive Directors resulting in casual vacancies on the Board. However, K-Electric cannot change its current Board composition in view of (i) an ad-interim order passed by the High Court of Sindh (SHC) in a suit filed by Al Jomaih Power Limited & Denham Investments Limited against IGCSPV 21 Limited and others; and (ii) a directive issued by Securities and Exchange Commission of Pakistan; restricting the Company to make any change in composition of the Board. However, operations and management of KE continues to operate.
- KE has a vast distribution network all over the city which is not a concession but 100% owned by KE. In the past, KE was granted a 20-year distribution license which expired in July 2023. With the ongoing changes in the power sector including Distribution (network) and Supply business being separate licensed activities under the NEPRA Act 1997 (as amended) and implementation of CTBCM, KE, during the year, filed separate license applications for Distribution and Supply businesses. A provisional renewal / extension in KE's distribution license was granted after the year-end in the interest of customers. KE remains engaged with NEPRA for timely issuance and finalization of its submitted license applications. The Company's favorable outcome of operational improvements, license extension and tariff petition as expected; would remain key rating factors.

**K-Electric Limited**
**Appendix I**

| <b>FINANCIAL SUMMARY</b>                        |                                  |             |             |
|---|----------------------------------|-------------|-------------|
|   | <i>(amounts in PKR billions)</i> |             |             |
| <b><u>BALANCE SHEET</u></b>                     | <b>FY21</b>                      | <b>FY22</b> | <b>FY23</b> |
| Fixed Assets                                    | 424.1                            | 489.2       | 580.2       |
| Investments                                     | 3.0                              | 2.9         | 2.9         |
| Stores, spares and loose tools                  | 16.1                             | 17.1        | 18.7        |
| Trade Debts                                     | 104.7                            | 136.8       | 104.3       |
| Other Receivables                               | 275.0                            | 375.2       | 239.4       |
| Cash & Bank Balances                            | 2.4                              | 2.8         | 7.1         |
| Total Assets                                    | 835.7                            | 1,060.1     | 1,024.7     |
| Trade and Other Payables                        | 353.9                            | 438.1       | 357.9       |
| Long Term Debt <i>(*incl. current maturity)</i> | 77.3                             | 175.40      | 216.8       |
| Short Term Debt                                 | 107.0                            | 107.5       | 92.9        |
| Total Debt                                      | 184.3                            | 283.1       | 309.8       |
| Paid Up Capital                                 | 96.3                             | 96.3        | 96.3        |
| Tier-1 Equity <i>(*excluding surplus)</i>       | 168.0                            | 180.5       | 153.7       |
| Total Equity <i>(*including surplus)</i>        | 224.0                            | 250.2       | 255.2       |
| <b><u>INCOME STATEMENT</u></b>                  | <b>FY21</b>                      | <b>FY22</b> | <b>FY23</b> |
| Revenue   | 325.0                            | 518.8       | 519.5       |
| Gross Profit                                    | 59.2                             | 68.5        | 52.8        |
| Operating Profit                                | 26.5                             | 20.8        | (7.8)       |
| Profit Before Tax                               | 15.3                             | 5.7         | (42.4)      |
| Profit After Tax                                | 12.0                             | 8.6         | (30.9)      |
| <b><u>RATIO ANALYSIS</u></b>                    | <b>FY21</b>                      | <b>FY22</b> | <b>FY23</b> |
| Gross Margin (%)                                | 18.2%                            | 13.2%       | 10.2%       |
| Net Margin (%)                                  | 3.7%                             | 1.6%        | -5.9%       |
| FFO   | 44.2                             | 49.4        | 16.6        |
| CFO   | 42.3                             | (25.7)      | 60.8        |
| FFO to Total Debt (%)                           | 24.0%                            | 17.0%       | 5.3%        |
| FFO to Long Term Debt (%)                       | 57.2%                            | 27.5%       | 7.6%        |
| CFO to Total Debt (%)                           | 22.9%                            | -9.5%       | 19.6%       |
| Debt Servicing Coverage Ratio (x)               | 2.25                             | 1.88        | 0.90        |
| Current Ratio (x)                               | 0.81                             | 0.91        | 0.80        |
| ROAA (%)  | 1.6%                             | 0.9%        | -           |
| ROAE (%)  | 7.5%                             | 4.9%        | -           |
| Gearing (x) (excluding revaluation surplus)     | 1.10                             | 1.57        | 2.02        |
| Debt Leverage                                   | 3.64                             | 4.49        | 5.01        |

| REGULATORY DISCLOSURE                      |   | Appendix II   |             |            |               |  |  |  |             |      |       |             |      |             |
|--|---|---------------|-------------|------------|---------------|--|--|--|-------------|------|-------|-------------|------|-------------|
| <b>Name of Rated Entity</b>                | K-Electric Limited  |               |             |            |               |  |  |  |             |      |       |             |      |             |
| <b>Sector</b>                              | Power   |               |             |            |               |  |  |  |             |      |       |             |      |             |
| <b>Type of Relationship</b>                | Solicited   |               |             |            |               |  |  |  |             |      |       |             |      |             |
| <b>Purpose of Rating</b>                   | STS-21 Issuance   |               |             |            |               |  |  |  |             |      |       |             |      |             |
| <b>Rating History</b>                      | <table border="1"> <thead> <tr> <th>Rating Date</th> <th>Short Term</th> <th>Rating Action</th> </tr> </thead> <tbody> <tr> <td colspan="3" style="text-align: center;"><b><u>RATING TYPE: STS-21 (Rs. 5b)</u></b></td> </tr> <tr> <td>06-Nov-2023</td> <td>A-1+</td> <td>Final</td> </tr> <tr> <td>20-Oct-2023</td> <td>A-1+</td> <td>Preliminary</td> </tr> </tbody> </table>   |               | Rating Date | Short Term | Rating Action | <b><u>RATING TYPE: STS-21 (Rs. 5b)</u></b> |  |  | 06-Nov-2023 | A-1+ | Final | 20-Oct-2023 | A-1+ | Preliminary |
| Rating Date                                | Short Term  | Rating Action |             |            |               |  |  |  |             |      |       |             |      |             |
| <b><u>RATING TYPE: STS-21 (Rs. 5b)</u></b> |   |               |             |            |               |  |  |  |             |      |       |             |      |             |
| 06-Nov-2023                                | A-1+  | Final         |             |            |               |  |  |  |             |      |       |             |      |             |
| 20-Oct-2023                                | A-1+  | Preliminary   |             |            |               |  |  |  |             |      |       |             |      |             |
| <b>Instrument Structure</b>                | <b>K ELECTRIC LIMITED – STS-21:</b> KE is raising up to Rs. 5b (inclusive of green shoe option of 1b) to finance working capital requirements of the company, by way of Short Term Sukuk issuance. Tenor of the STS is 6 months, with repayment by way of a single bullet payment. Indicative rate on the instrument would be 3-month KIBOR +50 bps.  |               |             |            |               |  |  |  |             |      |       |             |      |             |
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| <b>Probability of Default</b>              | 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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