RATING REPORT

K-Electric Limited – Short Term Sukuk-27

REPORT DATE:
October 10, 2024

RATING ANALYSTS:
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RATING DETAILS	Final	Preliminary
	Short-Term	Short-Term
K-Electric Limited – STS-27	A-1+	A-1+
Rating Date	*October 10, 2024*	*July 2, 2024*
Rating Action	*Final*	*Preliminary*

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

APPLICABLE METHODOLOGIES

Applicable Rating Criteria: Industrial Corporate
https://docs.vis.com.pk/docs/CorporateMethodology.pdf

Rating The Issue
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 (KE) is a public listed company incorporated in Pakistan in 1913 as KESC. Privatized in 2005, KE is a vertically integrated power utility in Pakistan supplying electricity to Karachi and its adjoining areas..

Profile of Chairman

Mark Gerard Skelton was appointed by the BOD as its Chairman in August 2022. Mark Skelton is a Managing Director with Alvarez & Marsal's (A&M's) Advisory practice in London. He has more than 20 years of experience in corporate finance and advisory. His primary areas of concentration are cross border assignments across different legal jurisdictions and waterfall classes.

Profile of CEO

Mr. Moonis Alvi was appointed CEO of KE in June 2018. Mr. Alvi has more than 30 years of diversified experience and has worked on the digitization, customer centricity and investments across the energy value chain Mr. Alvi joined KE in 2008 and has served as KE's Chief Financial Officer and other key positions and has played an integral role in the transformation of KE. He is also a Fellow member of the Institute of Chartered Accountants of Pakistan.

RATING RATIONALE

K-Electric (KE) is a public listed company incorporated in Pakistan in 1913 as KESC. Privatized in 2005, KE is avertically integrated power utility in Pakistan supplying electricity to Karachi and its adjoining areas. The majority shares (66.4%) of the Company are owned by KES Power, a consortium of investors including Al-Jomaih Power Limited of Saudi Arabia, National Industries Group (Holding), Kuwait, and the Infrastructure and Growth Capital Fund (IGCF). The Government of Pakistan is also a shareholder (24.36%) in the Company while the remaining are listed as free float shares.

Short Term Sukuk Issuance:

- KE has issued a rated, unsecured, privately placed Short-term Sukuk (STS-27) amounting to Rs. 5b to finance working capital requirements of the company on July 5, 2024.
- Tenor of the instrument is 6 months from the date of drawdown and will be redeemed in bullet at the expiry of tenor.
- Markup rate on the instrument is 6MKIBOR + 15 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 National Electric Power Regulatory Authority (NEPRA) to expedite the determination of pending quarterly tariff variations.
- 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 on a timeline basis. Going forward, additional loans will be required to fund planned investments in transmission and distribution, being undertaken over the next control period from FY24 to FY30, valued at Rs. 392b.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.

- However, given that the proposed tariff structure is yet to be approved, KE has been unable to finalize quarterly financial statements during the ongoing year. The Company has duly informed apex regulators, namely, SECP and NEPRA of the same.

Company Updates:

- With regards to the latest quarterly tariff adjustment for KE consumers, NEPRA has approved the adjustment till June 2023 via its decision dated August 02, 2024. KE has not filed any quarter adjustments for the period from July 2023 onwards in lieu of absence of KE's Multi Year Tariff (MYT). Moreover, the Company remains in continuous engagement with NEPRA to expedite the determination of MYT and pending quarterly tariff variations respectively.
- KE has filed separate tariff petitions for each of its business segments including Generation, Transmission, Distribution & Supply for the period FY24-30.For Generation Tariff, the approval for the same is in advanced stages and is expected to be issued in October 2024. Further, tariff petitions for Transmission, Distribution & Supply have been admitted by NEPRA and the public hearing for the same was held on June 27, 2024. Continued engagements are being done with NEPRA team to expedite the regulatory proceedings / approvals, and it is expected to be concluded soon.
- KE's Investment Plan of PKR 392bln has been approved for FY 2024 to FY 2030, which is aimed for 30% growth in customers, 20% increase in KE's share of renewables and another 30% reduction in power outages. Subject to third party studies and regulatory approvals, KE has planned a total addition of 2,272 MW including renewables of approximately 1,282 MW, by FY30. Moreover, the management expects that the overall procedure will be completed by Dec'24.
- KE's Power Acquisition Programme (PAP) for the period FY 2024 to FY 2028 has been approved by NEPRA on May 20, 2024 to develop a long-term capacity expansion plan to meet the energy demand in a reliable, sustainable and cost-effective manner as the Supplier of Last Resort (SoLR) for its licensed service territory.
- The overall control of K-Electric Limited ("KE" or "the Company") vests in 13-member Board of Directors (BoD), including the CEO, where majority is nominated by KES Power Limited (KESP), KE's holding company. In addition to KESP's nominees, the Board also comprises of the directors nominated by Government of Pakistan (GoP) and an independent director. However, in October 2022, resignation of 3 directors nominated by KESP resulted in casual vacancies on the Board which cannot be filled by the Company as the is restricted from making change in its current Board composition in view of (i) An ad-interim order of the High Court of Sindh was passed on 21 October 2022, in the suit filed by Al Jomaih Power Limited & Denham Investments Limited against IGCF SPV 21 Limited and others whereby no change shall be affected in the present Board of the Company; and (ii) A directive under section 125 of the Securities Act, 2017 was issued by Securities and Exchange Commission of Pakistan on 08 November 2022 according to which the composition of the current BoD of KE shall not be changed, till further orders of the Commission. However, operations and management of KE continues to operate.
- For distribution and supply of electric power services in its territory, KE's Distribution & Supply Licenses have been renewed by NEPRA for the next 20 years, effective from 19th January 2024.
- Shanghai Electric Power (SEP) had entered into a Sale-and-Purchase Agreement (SPA) with KES Power Limited (holding company), to acquire 66.4% shareholding of KE during Oct'16. SEP issued a fresh Public Announcement of Intention (PAI) for the acquisition during July'23 which was valid for 180 days and was followed by a 90-day extension received during Jan'24. However, the extension expired during April'24 as regulatory approvals pertaining to the transaction remained pending. As per applicable law, SEP is entitled to make a fresh PAI at any time going forward.
- KE manages its working capital requirements through a mix of internally generated cash and short term borrowings. Post signing of the power purchase agreement with CPPA-G whereby KE is now authorized to procure upto 2,000 MW of electricity from NTDC, KE has also signed another agreement with GoP for Tariff Differential Subsidy whereby KE can net off the NTDC invoices with the subsidy amount and pay only the differential amount. The arrangement has been secured via a master collection account dedicated for payments to CPPA-G. As per management, the actual position of cashflows and the debt profile of the Company is in a sound position and it's expected that the same trend will continue going forward. The approval of the Investment Plan of PKR 392bln by NEPRA for rehabilitation of the transmission and distribution network of KE is expected to

contribute to a surge in debt post finalization of MYT. However, KE has MCA structures that are already used to pay back long term lenders and they will continue to do the same in the future.

- KE is continuously diversifying its fuel mix and generating power from greener sources by initiating renewable power projects. The Company has received 15 bids for its 150 MW solar projects in Winder and Bela, Balochistan. This progress would enable the Company to reach its target of 30% renewable energy in its generation mix by 2030. KE announced the receipt of seven bids for Pakistan's first 220 MW hybrid wind/solar project in Dhabeji Sindh. Additionally, the planned 270 MW GOS Solar Renewable Project will further support this objective, integrating wind, solar, and hydel power in KE's fleet..
- Going forward, materialization of favorable outcomes in terms of operational improvements, tariff petitions and planned energy projects would remain key rating factors.

K-Electric Limited Appendix I

FINANCIAL SUMMARY			*(amounts in PKR billions)*
BALANCE SHEET	**FY21**	**FY22**	**FY23**
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 *(*incl. current maturity)*	77.3	175.5	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 *(*excluding surplus)*	168.0	180.5	153.7
Total Equity *(*including surplus)*	224.0	250.2	255.2
INCOME STATEMENT	**FY21**	**FY22**	**FY23**
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	5.6	(42.4)
Profit After Tax	12.0	8.5	(30.9)
RATIO ANALYSIS	**FY21**	**FY22**	**FY23**
Gross Margin (%)	18.2%	13.2%	10.2%
Net Margin (%)	3.7%	1.6%	-5.9%
FFO	44.2	52.3	16.6
CFO	42.3	(25.7)	60.8
FFO to Total Debt (%)	24.0%	18.5%	5.3%
FFO to Long Term Debt (%)	57.2%	29.8%	7.6%
CFO to Total Debt (%)	22.9%	-9.1%	19.6%
Debt Servicing Coverage Ratio (x)	2.25	1.96	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		
Name of Rated Entity	K-Electric Limited		
Sector	Power		
Type of Relationship	Solicited		
Purpose of Rating	STS-27 Issuance		
Rating History	**Rating Date**	**Short Term**	**Rating Action**
	RATING TYPE: STS-27 (Rs. 5b)		
	10/Oct/2024	A-1+	Final
	2/July/2024	A-1+	Preliminary
Instrument Structure	**K ELECTRIC LIMITED – STS-27:** KE has raised Rs. 5b to finance its working capital requirements of the company by way of Short Term Sukuk issuance at a face value of Rs. 1m each or in multiples thereof. Tenor of the STS is 6 months, with repayment by way of a single bullet payment. Indicative rate on the instrument is 6-month KIBOR + 15 bps p.a.		
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.		
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