RATING REPORT

Kot Addu Power Company Limited

REPORT DATE:
January 12, 2023

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+
Entity Rating Action	*Downgrade*		*Maintained*	
Rating Outlook	*Stable*		*Rating Watch-Developing*	
Entity Rating Date	*Jan 12, 2023*		*Dec 9, 2021*	

COMPANY INFORMATION

Incorporated in 1996	**External auditors:** A. F. Ferguson & Co. Chartered Accountants
Public Limited Company	**Chairman:** Lt. General (Retd.) Sajjad Ghani **CEO:** Mr. Aftab Mahmood Butt
Key Shareholders (with stake 5% or more):	
WAPDA – 40.3%	
KAPCO Employees Empowerment Trust – 5.5%	

APPLICABLE METHODOLOGY(IES)

VIS Entity Rating Criteria: Corporate Rating Methodology (August, 2021)
https://docs.vis.com.pk/docs/CorporateMethodology202108.pdf

Kot Addu Power Company Limited

RATING RATIONALE

Kot Addu Power Company Limited ('KAPCO' or 'the Company'), was incorporated in Pakistan on April 25, 1996 as a public limited company under the Companies Ordinance, 1984 (now Companies Act, 2017). The Company was listed on April 18, 2005 on Pakistan Stock Exchange Limited. The principal activities of the Company are to own, operate and maintain a multi-fuel fired power station with 15 generating units, featuring a nameplate capacity of 1,600 MW in Kot Addu, District Muzaffargarh, Punjab, Pakistan.

Business Update

Update on PPA, Generation License & CBTCM

- The PPA which was initially for a term of 25 years was due to expire on June 26, 2021, however, the Company signed a Master Agreement and the Third Amendment to the Power Purchase Agreement (PPA) on February 11, 2021, gaining an extension that has also expired on 24th October 2022.
- The Company sought an interim tariff while it has applied to the National Electric Power Regulatory Authority (NEPRA) for a new tariff in order to supply electricity to Central Power Purchasing Agency (CPPA-G) for a span of 5 years. As NEPRA is yet to arrive at a conclusion regarding the tariff petition and the original PPA, the Company has solicited NEPRA to grant interim tariff approval for meeting technical, operational and dispatch requirements of power purchaser and the system.
- The Company's generation license was renewed for a period of 3 years, which will expire on September 21st, 2024, considering the remaining useful life and critical importance of the Power Plant in the system.
- The management is confident of getting an extension of PPA, based on the following reasons:
  - Issuance of new generation license by NEPRA for a period of 3 years.
  - National Transmission & Dispatch Company (NTDC) submitted a revised Indicative Generation Capacity Expansion Plan (IGCEP) 2022-31 to NEPRA, which included the Company's Power Plant in the System till FY26, citing system constraints.
  - The Company's Power Plant being able to run on multi-fuel while also having black start facility.
  - KAPCO's strategic location and it capability of being major feeding source for distribution companies in Central and Lower Punjab.
  - The remaining useful life of the Power Plant is at least 10 years as per the life assessment study carried out by an independent foreign consultant in June 2021.
  - KAPCO's requirement for the national grid is evident from the recent load levels posted by the plant over the past 3-year period.
  - Government of Pakistan (GoP) being the major shareholder of the Company through WAPDA.
- NEPRA has formally introduced Competitive Trading Bilateral Contracts Market (CTBCM) for a trail period of 6 months. This allows Power Producers to participate in the Market by selling electricity to Bulk Power Consumers. The Company intends to reap benefits from CTBCM once it is fully implemented.

Operational Update

Table 1: Operational Metrics

	FY19	FY20	FY21	FY22
Load Factor (%)	42%	30%	30%	42%
Energy Dispatched (GWH)	4,961	3,477	3,562	4,980
Annual Dependable Capacity (MWH)	11,756	11,788	11,756	11,756
Availability	91.80%	88.90%	85.6%	90.0%
Thermal Efficiency	44.00%	44.40%	44.5%	43.4%

OVERVIEW OF THE INSTITUTION

KAPCO was incorporated in Pakistan on April 25, 1996 as a public limited company under the Companies Ordinance, 1984 (now Companies Act, 2017). The Company was listed on April 18, 2005 on Pakistan Stock Exchange Limited. The Company has a plant site, a corporate office and a registered office. The Company has a plant site at Kot Addu, a corporate office located in Lahore and registered office located in Islamabad.

Profile of the Chairman

Lt General (Retd.) Sajjad Ghani was appointed a Director on August 17, 2022. General Ghani is a professional engineer and retired soldier, who has pursued two parallel career streams for over last four decades. He obtained Bachelor of Engineering Degree from Military College of Engineering in 1984. He was awarded Master's Degree in Civil Engineering from University of Engineering and Technology, Lahore in 1990. He has served Commander of Corps Engineers and Quarter Master General Pakistan Army where numerous mega construction projects were executed under his supervision.

Profile of the CEO

Management team is headed by Mr. Aftab Mahmood Butt who is the Chief Executive Officer. Mr. Aftab is a chartered accountant by profession and previously served on the boards of Central Power Purchasing Guarantee Limited & Lahore Stock Exchange Limited. His other professional experience includes the position of Member

Finance & Secretary Board in the Corporate and Industrial Restructuring Corporation, Ministry of Finance, Government of Pakistan.

- The energy dispatch by the Company was lowest in a decade during FY20 owing to decrease in electricity demand from commercial sector. Subsequent to remaining flat in FY21, it has picked up in FY22 with a 40% increase from preceding year.

Table 2: Balance Sheet (Extract)

	June'20	Jun'21	Jun'22	Sep'22
Assets	**134,523**	**152,234**	**136,761**	**121,750**
- **Non-Current Assets**	4,145	3,521	2,984	2,764
- **Stock in Trade**	2,701	5,922	6,236	11,532
- **Trade Debts**	119,904	104,622	62,154	44,531
- **Investments**	-	25,670	54,067	50,939
- **Cash & bank Balances**	835	1,284	1,018	980
- **Others**	6,938	11,214	10,301	11,183
Liabilities	**74,173**	**87,010**	**68,165**	**51,044**
- ***Debt***	44,088	36,268	37,374	32,737
- **Contract Liability**	-	19,128	4,613	954
- **Trade Payables**	20,785	17,178	21,470	12,298
- **Others**	9,301	14,436	2,853	3,545
Equity	**60,351**	**65,224**	**68,596**	**70,705**

- As can be ascertained form the Balance Sheet extract above, the Company's debt, net of liquid assets, is essentially zero.
- Given sizable clearance of trade debts in Q2'FY22, in line with the agreement signed with the GoP, overall quantum of trade debts is lower on a timeline. The aging profile of trade debts as of Jun'22 was also relatively better, as merely 3.7% of the receivables were past due beyond 60 days (Jun'21: 62.9%).

Table 3:Profitability Margins

	FY20	*FY21*	*FY22*	*Q1'FY23*
Sales	**71,543**	**50,349**	**136,600**	**22,890**
Less: Cost of Sales	**50,065**	**45,098**	**128,068**	**21,314**
- *Energy Purchase Revenue (net of Sales Tax)*	45,894	41,694	122,958	19,282
- *Capacity Purchase Price – net*	25,650	27,943	13,641	3,608
Gross Profit	**21,478**	**5,251**	**8,532**	**1,576**
Gross Margin	**30.0%**	**10.4%**	**6.2%**	**6.9%**
Net Margin	**33.0%**	**20.3%**	**7.2%**	**9.2%**

Table 4: Cash Flow Coverage Indicators

	FY20	*FY21*	*FY22*	*Q1'FY23*
FFO	**27,489**	**25,581**	**(13,654)**	**(2,511)**
FFO to Total Debt (%)	**62%**	**71%**	**(37%)**	**(31%)***
DSCR (x)	**3.45**	**4.03**	**(1.05)**	**(0.73)***
(Stock in trade + trade debts)/ ST Debt (x)	**2.78**	**3.05**	**1.83**	**1.71**
**** Annualized***				

- As per the Third Amendment to PPA, the Company created a Contract Liability of Rs. 19.3b, which has been almost fully (~95%) amortized during the period Jun'21-Sep'22. As a result of the amortization, the cashflow coverage indicators have been negatively impact. However, as contract liability has been fully amortized, the trend will not continue going forward.
- Going forward, in the Integrated Generation Capacity Expansion Plan 2022-31, NEPRA has indicated that KAPCO 3 (300 MW) would be fully retired, while KPACO 1 (400MW) and KAPCO2 (900MW) would remain operational, with capacity utilization expected at 35.3% and 11.9% respectively.
- As per NEPRA assumptions, minimum dispatch of 500 MW from Existing KAPCO CCPP (Block-I and Block-II) in the months of May to September up till year 2025 has been considered, beyond its PPA expiry i.e., Oct. 2022, owing to network requirements/constraints, whereas, the remaining capacity (Block-III) has been retired as per PPA expiry. NEPRA also states that, "It is pertinent to mention that the requirement of KAPCO beyond its PPA expiry will be assessed in ongoing Transmission System Expansion Plan (TSEP), accordingly competent forum will be approached, after consensus among concerned stakeholders i.e., NTDC, CPPA-G and KAPCO, for PPA extension or otherwise and the same will be considered in next iteration of IGCEP".

Rating Drivers

Rating incorporates ownership by a State-Owned Entity (SOE) and strategic importance of KAPCO to the national grid

The rating takes into account ownership profile of the Company, with majority shareholding being held by WAPDA. Even though the Company's PPA with the Government of Pakistan (GoP) has expired in Oct'22, the strategic importance of KAPCO to the national grid is evident from NEPRA's IGCEP 2021-22, wherein the regulator has indicated that KAPCO will remain part of the system till FY26 mainly to cater for system constraints.

Given non-renewal of PPA, demand risk has been incorporated in the assigned rating
The extended PPA has expired in October 2022. As per the IGCEP, the Company will continue to operate till FY25, on account of system constrains of Pakistan's national grid, with limited capacity utilization. Accordingly, given changes to the Company's business risk profile, assigned rating of KAPCO has been revised.

Rating is supported by Conservative Capital Structure
Over the years, KAPCO has entirely repaid its long term debt, and the debt on the books is essentially short term in nature used for financing working capital requirements, particularly because of delayed release of payments from CPPA-G. This does not affect KAPCO's profitability, as the Company also books interest income on these receivables. However, it results in inflating trade debts and debt utilization of the Company. Credit risk on these receivables is viewed as low, given that these are sovereign guaranteed. The rating also incorporates sizable liquid assets on KAPCO's balance sheet, as a result of which net debt of the Company is nil, while these liquid assets also generate secondary income for the Company.

Kot Addu Power Company Limited **Annexure I**

FINANCIAL SUMMARY					*(amounts in PKR millions)*
BALANCE SHEET	**Jun'19**	**Jun'20**	**Jun'21**	**Jun'22**	**Sep'22**
Fixed Assets	6,337	4,106	3,068	2,237	2,007
Long term Investments	-	-	-	-	-
Stock-in-Trade	9,466	2,701	5,922	6,236	11,532
Trade Debts	115,798	119,904	104,622	62,154	44,351
Cash & Bank Balances	1,350	835	1,284	1,018	980
Total Assets	139,267	134,523	152,234	136,761	121,750
Trade and Other Payables	40,139	20,785	17,178	21,470	12,298
Long Term Debt	38	25	11	3	3
Short Term Debt	54,180	44,062	36,257	37,370	32,734
Total Debt	54,218	44,088	36,268	37,374	32,737
Paid Up Capital	8,803	8,803	8,803	8,803	8,803
Total Equity	41,161	60,351	65,224	68,596	70,705
	FY19	**FY20**	**FY21**	**FY22**	**Q1'FY23**
INCOME STATEMENT					
Net Sales	84,831	71,543	50,349	136,600	22,890
Gross Profit	14,205	21,478	5,251	8,532	1,576
Operating Profit	27,269	41,412	17,519	19,897	5,027
Profit Before Tax	18,963	32,954	14,411	15,524	3,149
Profit After Tax	13,112	23,613	10,229	9,894	2,110
RATIO ANALYSIS	**FY19**	**FY20**	**FY21**	**FY22**	**Q1'FY23**
Gross Margin (%)	16.7%	30.0%	10.4%	6.2%	6.9%
Net Margin (%)	15.5%	33.0%	20.3%	7.2%	9.2%
Net Working Capital	36,193	64,722	75,543	67,494	70,516
Trade debts/Sales	136.5%	167.6%	207.8%	45.5%	48.4%*
FFO	18,608	27,489	25,581	(13,654)	(2,511)
FFO to Total Debt (%)	34%	62%	71%	(37%)	(31%)*
Debt Servicing Coverage Ratio (x)	3.70	3.45	4.03	(1.05)	(0.73)*
Current Ratio (x)	1.38	1.99	2.03	2.02	2.45
Stock+ Trade Debts/STD	231.2%	278.3%	304.9%	183.0%	170.7%
Gearing (x)	1.32	0.73	0.56	0.54	0.46
Leverage (x)	2.38	1.23	1.33	0.99	0.72
ROAA (%)	9.4%	17.2%	7.1%	6.8%	6.5%*
ROAE (%)	34.4%	46.5%	16.3%	14.8%	12.1%*

**Annualized*

ISSUE/ISSUER RATING SCALE & DEFINITIONS Appendix II

VIS Credit Rating Company Limited

RATING SCALE & DEFINITIONS: ISSUES / ISSUERS

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: 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.vis.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.vis.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.vis.com.pk/images/policy_ratings.pdf

'SD' Rating: An 'SD' rating is assigned when 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 DISCLOSURES — Appendix III

Name of Rated Entity	Kot Addu Power Company Limited
Sector	Power
Type of Relationship	Solicited
Purpose of Rating	Entity Ratings

Rating History

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
		RATING TYPE: ENTITY		
01/12/2023	AA	A-1	Stable	Downgrade
12/9/2021	AA+	A-1+	Rating Watch Developing	Maintained
12/14/2020	AA+	A-1+	Rating Watch Developing	Maintained
12/02/2019	AA+	A-1+	Stable	Reaffirmed
12/31/2018	AA+	A-1+	Stable	Reaffirmed
12/18/2017	AA+	A-1+	Stable	Reaffirmed
11/28/2016	AA+	A-1+	Stable	Reaffirmed
11/20/2015	AA+	A-1+	Stable	Reaffirmed
12/29/2014	AA+	A-1+	Stable	Reaffirmed
9/20/2013	AA+	A-1+	Stable	Reaffirmed
5/03/2012	AA+	A-1+	Stable	Reaffirmed
2/21/2011	AA+	A-1+	Stable	Reaffirmed
		RATING TYPE: CP/STS		
09/09/2020		A-1+		Preliminary

Instrument Structure	N/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.
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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Due Diligence Meetings Conducted

Name	Designation	Date
Mr. Zubair Aslam	Financial Controller	November 11, 2022
Mr. Nabeel Ahmed	Treasury Manager	