# RATING REPORT

## Nishat Chunian Power Limited

**REPORT DATE:**
September 27, 2023

**RATING ANALYSTS:**

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| RATING DETAILS | | |
|---|---|---|
| **Rating Category** | **Latest Rating** | **Previous Rating** |
| **Entity** | **A+/A-2** | **A+/A-2** |
| ***Rating Date*** | *September 27, 2023* | *May 16, 2022* |
| **Rating Outlook** | Stable | Stable |

| COMPANY INFORMATION | |
|---|---|
| **Incorporated in 2007** | **External Auditors:** Riaz Ahmed & Company & Co., Chartered Accountants |
| **Public Listed Company** | **Chairman:** Mr. Muhammad Ashraf |
| **Key Shareholders (with stake 5% or more):** | **Chief Executive Officer:** Mr. Farrukh Ifzal |
| *Mr. Shahzad Saleem – 17.64%* | |

| APPLICABLE METHODOLOGY(IES) |
|---|
| **Applicable Rating Criteria:**<br>**Corporates (May 2023) https://docs.vis.com.pk/docs/CorporateMethodology.pdf**<br>**Rating Scale & Definitions https://docs.vis.com.pk/docs/VISRatingScales.pdf** |

# Nishat Chunian Power Limited

| OVERVIEW OF THE INSTITUTION | RATING RATIONALE |
|---|---|

*Nishat Chunian Power Limited (NCPL), established as an IPP under the Power Policy 2002, was incorporated as a public limited company in February, 2007.*

**Profile of Chairman**

*Mr. Muhammad Ashraf is associated with the Nishat Chunian Group for more than 25 years in different important positions. He possesses a rich experience playing a pivotal & inspirational role with the Group. Mr. Muhammad Ashraf is currently serving as Chairman of the Board of Directors of Nishat Chunian Power Limited since March 2022.*

**Profile of CEO**

*Mr. Farrukh Ifzal has been associated with Nishat Chunian Group since 1988 and has been serving in various capacities. Mr. Ifzal is also present on the board of Nishat Chunian Limited and Pakgen Power Limited. He is a Fellow Member of the Institute of Chartered Accountants of Pakistan.*

Nishat Chunian Power Limited ('NCPL' or 'the company') was incorporated in 2007 as a public limited company with primary activity of operating a 200 MW residual fuel oil (RFO) based power plant in District Kasur, Punjab. The company has 25-year Power Purchase Agreement (PPA) entailing 'take or pay' provision with Central Power Purchasing Agency-Guarantee (CPPA-G) with net production levels of 195.72 MWh (megawatt per hour). The project started commercial operations in 2010.

**Key Rating Drivers**

**Long association with group and experienced management team:** Ratings draw comfort from the company's long historic association with Nishat Chunian Group (NCG), one of the leading groups in Pakistan with sizable financial strength and presence in textile and power generation. On August 10, 2022, according to a Scheme of Compromises, Arrangement and Reconstruction (Under Sections 279 to 283 and 285 of the Companies Act, 2017), the company ceased to be the subsidiary of Nishat Chunian Limited (NCL) and its shares were transferred amongst members of NCL. Thereafter, the company is operating as a standalone entity.

**Ratings derive support from 25-year Power Purchase Agreement (PPA) with CPPA-G while 'take or pay' arrangement alleviates off-take risk:** The company currently enjoys 'take or pay' (guaranteed payment on long-term basis if capacity is made available) tariff arrangement with CPPA-G. In addition, 'Implementation Agreement' (IA) provides sovereign guarantee for cash flows, contingent upon adherence to stipulated performance benchmarks. As per NTDC's (National Transmission & Despatch Company) revised merit order issued on Sep'23, NCPL's standing in the merit order was 50/74 (Jun'23: 31/73, Jun'22: 67/124). Revenue from CPPA-G is invoiced on a monthly basis as per tariff structure. In case of delayed payments, mark-up is charged on the overdue amount.

**Operations & Maintenance (O&M):** NCPL has an experienced in-house O&M team, which has demonstrated track record of compliance with both availability and operational efficiency since the expiration of agreement with O&M contractor in 2015. Given that an in-house team is undertaking O&M, there is no recourse to liquidated damages in case plant's performance falls below parameters stipulated in PPA. Comfort is drawn from the experience of senior management members of the in-house O&M team and track record of compliance with both availability efficiency since the expiration of the O&M agreement with Wartsila Pakistan (Pvt.) Limited in January, 2015.

**Limited fuel supply risk:** RFO based projects account for 6.20% share in power supplied to the national grid meanwhile the cost of power generation from RFO based projects was highest vis-à-vis other sources reaching Rs. 35.6984 per unit in FY23. NCPL procures fuel from different local vendors whereas, the price risk is mitigated since the cost is a pass-through item as per the tariff subject to achieving the PPA stipulated parameters.

**PPA Amendment Agreement:** On 11 February 2021, the company entered into a Novation Agreement to the PPA with NTDC and CPPA-G, whereby, NTDC irrevocably transferred all of its rights, obligations and liabilities under the PPA to CPPA-G and thereafter, NTDC ceased to be a party to the PPA, and CPPA-G became a party to the PPA in place of NTDC. Further, on the same day, the company entered into the PPA Amendment Agreement, whereby NCPL and the Committee for Negotiation with IPPs formed by Government of Pakistan (GoP) executed a Memorandum of Understanding (MoU). This majorly included conversion to 'take and pay' subject to mutual agreement of the parties when Competitive Trading Arrangement (CTA) is implemented and becomes fully operational; sharing of future savings in fuel and O&M and reduction in delayed payment rate and settlement of outstanding receivables. Additionally, dispute relating to withheld capacity payment of Rs. 966.2m was also settled by extending the PPA term by 75 days. Therefore, the existing term of the PPA Agreement will end on 4 Oct, 2035. Lastly, amendments in tariff components as a result of the aforementioned agreement have been applied from Jun 30, 2022 onwards.

**Profitability:** In FY23, the plant's availability factor stood at 91.40% (FY22: 91.54%) whereas capacity factor declined to 22.52% (FY22: 51.47%) on the account of downturn in demand of power as a result of overall economic slowdown. Power dispatched to the CPPA-G declined by 56.2% (FY23: 386,127 MWh, FY22: 882,453 MWh). Resultantly, net sales fell to Rs. 18.2b in FY23 as compared to Rs. 25.4b in FY22. Moreover, NCPL recorded higher markup on delayed payments at Rs. 2.2b (FY22: Rs. 1.6b) in FY23. As a result of higher proportion of Capacity Purchase Price (CPP) component to 19.8% vis-à-vis 9.5% in preceding year, NCPL's gross margin increased to 27.8% (FY22: 14.0%, FY21: 32.4%) in FY23.

Operating expenses remained largely stable. Other income amounted to Rs. 113.1m (FY22: Rs. 160.5m), which largely comprised scrap sales and interest on Govt. treasury bills. Finance cost stood at Rs. 868.3m (FY22: Rs. 884.2m, FY21: Rs. 984.4m) in FY23. Tax charge has remained minimal as the company's profits are exempt from taxation and only other income is taxable. In FY23, net profitability was recorded higher at Rs. 3.9b (FY22: Rs. 2.5b) with higher net margins of 21.7% (FY22: 9.8%, FY21: 21.5%).

With increase in the country's power generation capacity base, addition of new power producers that either operate out of merit order (renewable energy projects) or rank higher in the merit order, dispatch may be affected. Moreover, power demand is expected to decrease owing to current macroeconomic challenges including inflation, power prices hikes and slower economic growth.

**Liquidity Profile:** Trade receivables stood at Rs. 13.75b (FY22: Rs. 13.72b) as at Jun 30, 2023. Post signing PPA amendment, NCPL received settlement of outstanding old receivables to the tune of Rs. 14.8b in FY22. However, circular debt has continued to stress short-term liquidity in the ongoing year, as witnessed in increase in overdue receivables beyond 6 months period. Trade receivables were reported higher at Rs. 16.5b as on Aug 31, 2023, out of which Rs. 8.4b were overdue. Aging profile of these overdue receivables indicates that ~37% were due for less than 3 months, ~39% fall within 3 to 6 months bracket while ~24% were outstanding for more than 6 months. Nonetheless, these receivables are due from CPPA-G and are considered good. These are secured by a guarantee from the GOP under the IA and are in the normal course of business and interest free. However, delayed payment mark-up at the rate of three months KIBOR plus 2.00% per annum for first sixty days and three months KIBOR plus 4.50% per annum after first sixty days, each compounded semi-annually, is charged in case the amounts are not paid within due dates. The rate of delayed payment mark-up charged during the year on outstanding amounts ranged from 16.80% to 26.58% (2022: 11.53% to 19.53%) per annum. Fuel stock held by the company stood lower at Rs. 808.9m (FY22: Rs. 2.25b) in line with reduced demand from power purchaser. Trade and other payables increased to Rs. 2.3b (FY22: Rs. 1.0b) largely on account of higher outstanding creditors. Current ratio also improved to 5.19x (FY22: 2.20x).

Given higher profitability, FFO (funds from operations) increased to Rs. 4.7b (FY22: Rs. 3.3b) in FY23. This, along with significant decline in outstanding short-term borrowing led to improvement in FFO to total debt ratio. Similarly, DSCR (debt service coverage ratio) has remained sizable due to higher FFO and no long-term repayments.

In March 2020, Committee for the Power Sector Audit, Circular Debt Resolution and Future Roadmap constituted by Ministry of Energy alleged that savings were made by the 'IPPs', including NCPL, in the tariff components. On 11 February 2021, the company and CPPA-G have signed 'Master Agreement' and 'PPA Amendment Agreement' wherein it has been agreed that the dispute will be resolved through arbitration under the 'Arbitration Submission Agreement' between the company and GoP. On 15 November 2021, the Company has authorized GoP/CPPA-G to retain Rs. 8.36b of its trade debts until the Arbitration Tribunal renders the Award which shall be final and binding. During FY23, Arbitration Tribunal has been constituted under the terms of 'Arbitration Submission Agreement', however formal adaptation of mutually agreed Terms of Reference is in process. Management believes that there are strong grounds that the matter will ultimately be decided in the company's favor. Furthermore, its financial impact cannot be reasonably estimated at this stage, hence, no provision in this respect has been made in these financial statements.

**Capitalization:** The equity base of the company amounted to Rs. 24.3b (FY22: Rs. 24.0b) at end-FY23. Despite higher profitability, equity growth was not that significant owing to dividend payout amounting Rs. 3.7b in FY23. The debt profile included only short-term borrowings to meet working capital requirements; short-term financing stood substantially lower at Rs. 975.1m (FY22: Rs. 10.9b) as of June 30, 2023. Aggregate working capital facilities from various commercial banks, amounting to Rs. 13.95b (FY22: Rs. 13.56) were available to the company at end-FY23. As a result, gearing ratio and leverage were reported lower at 0.04x (FY22: 0.45x) and reached 0.15x (FY22: 0.50x), respectively. Leverage indicators are expected to remain manageable, going forward.

**Composition of the Board:** As of June 30, 2023, the Board of Directors (BoD) had seven members including CEO, Chairman and two independent directors. Following the resignation of Ms. Samina Aslam on August 29, 2023, Ms. Nadia Bilal was appointed as a female director on September 14, 2023. The BoD has developed a vision/mission statement, overall corporate strategy and significant policies of the company. All the powers of the BoD have been duly exercised and decisions on relevant matters have been taken by the Board/shareholders as empowered by the relevant provisions of the Companies Act, 2017 (the Act) and the Regulations. The BoD held four meetings during FY23 to oversee effective corporate governance of NCPL. Overall attendance during Board meetings remained satisfactory.

**Environmental, Social, and Corporate Governance (ESG):** NCPL has ESG measures put in place to manage financial and non-financial risks. EHS (environment, health and safety) policy is made to ensure safety of employees and physical assets, and minimize environmental impact. The company conducts quarterly monitoring of its air, noise and

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|---|---|
| | water quality since starting operations in 2010. NCPL has an Environment Management Plan (EMP) to enable safety of oil transportation and control of emissions. Tree plantation is also done, in line with CSR initiatives. NCPL disposes of carbon waste in accordance with local rules and regulations. Therefore, ESG practices at NCPL are considered feasible. |

## Nishat Chunian Power Limited Appendix I

| FINANCIAL SUMMARY | | | (Amounts in PKR millions) |
|---|---|---|---|
| **BALANCE SHEET** | **FY21** | **FY22** | **FY23** |
| Property, plant and equipment | 9,856.2 | 9,461.0 | 9,478.8 |
| Stock in Trade | 868.7 | 2,254.7 | 808.9 |
| Stores & Spares | 393.0 | 445.6 | 628.9 |
| Trade debts | 20,441.9 | 13,718.1 | 13,747.7 |
| Advances, prepayments and other receivables | 870.4 | 1,510.2 | 1,308.8 |
| Cash and bank balances | 297.8 | 21.0 | 1,406.4 |
| Income tax receivable | 52.9 | 61.3 | 45.6 |
| Short-term investments | 311.9 | 8,609.0 | 361.8 |
| Other assets | 2.5 | 2.1 | 1.1 |
| **Total Assets** | **33,095.4** | **36,082.9** | **27,787.8** |
| Trade and Other Payables | 1,284.5 | 1,016.0 | 2,341.4 |
| Other Liabilities | 261.3 | 216.7 | 208.6 |
| Long Term Debt | 51.7 | 17.3 | - |
| Short Term Debt | 10,022.7 | 10,853.0 | 975.1 |
| **Total Debt** | **10,074.5** | **10,870.3** | **975.1** |
| **Total Liabilities** | **11,620.2** | **12,103.0** | **3,525.2** |
| Paid up Capital | 3,673.5 | 3,673.5 | 3,673.5 |
| Unappropriated Profit | 17,801.8 | 20,306.0 | 20,588.6 |
| **Total Equity** | **21,475.3** | **23,979.5** | **24,262.1** |
| | | | |
| **INCOME STATEMENT** | **FY21** | **FY22** | **FY23** |
| Net Sales | 11,643.3 | 25,416.0 | 18,220.8 |
| Gross Profit | 3,770.2 | 3,557.7 | 5,058.0 |
| Finance Cost | (984.4) | (884.2) | (868.3) |
| Profit/(Loss) Before Tax | 2,509.3 | 2,504.7 | 3,957.2 |
| **Profit After Tax** | **2,509.3** | **2,503.8** | **3,956.6** |
| | | | |
| **RATIO ANALYSIS** | **FY21** | **FY22** | **FY23** |
| Gross Margin (%) | 32.40% | 14.00% | 27.80% |
| Net Margin (%) | 21.60% | 9.90% | 21.70% |
| ROAA (%) | 7.80% | 7.20% | 13.80% |
| ROAE (%) | 12.40% | 11.00% | 16.70% |
| FFO (Funding from operations) | 3,340.4 | 3,387.0 | 4,795.4 |
| FFO/Long-term Debt (x) | 64.5 | 193.3 | NM |
| FFO/Total Debt (x) | 0.33 | 0.31 | 4.92 |
| Gearing (x) | 0.47 | 0.45 | 0.04 |
| Debt Leverage (x) | 0.54 | 0.5 | 0.15 |
| Current Ratio (x) | 2.00 | 2.20 | 5.20 |
| DSCR (Debt service coverage ratio) (x) | 1.85 | 4.46 | 6.16 |
| Cash conversion cycle (CCC) (days) | 598 | 252 | 272 |

<table>
<tr><th>REGULATORY DISCLOSURES</th><th colspan="5">Appendix II</th></tr>
<tr><td>Name of Rated Entity</td><td colspan="5">Nishat Chunian Power Limited</td></tr>
<tr><td>Sector</td><td colspan="5">Power Generation</td></tr>
<tr><td>Type of Relationship</td><td colspan="5">Solicited</td></tr>
<tr><td>Purpose of Rating</td><td colspan="5">Entity Rating</td></tr>
<tr><td rowspan="4">Rating History</td><td>Rating Date</td><td>Medium to Long Term</td><td>Short Term</td><td>Rating Outlook</td><td>Rating Action</td></tr>
<tr><td colspan="5">RATING TYPE: ENTITY</td></tr>
<tr><td>27/09/2023</td><td>A+</td><td>A-2</td><td>Stable</td><td>Reaffirmed</td></tr>
<tr><td>16/05/2022</td><td>A+</td><td>A-2</td><td>Stable</td><td>Initial</td></tr>
<tr><td>Statement by the Rating Team</td><td colspan="5">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.</td></tr>
<tr><td>Probability of Default</td><td colspan="5">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.</td></tr>
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<tr><td rowspan="5">Due Diligence Meeting Conducted</td><td colspan="2">Name</td><td colspan="2">Designation</td><td>Date</td></tr>
<tr><td colspan="2">Mr. Ubaid Ullah Azam</td><td colspan="2">Manager Finance</td><td>23 Aug, 2023</td></tr>
<tr><td colspan="2">Ms. Rameen Sarwar</td><td colspan="2">Deputy Manager Finance</td><td>23 Aug, 2023</td></tr>
<tr><td colspan="2">Mr. Waqas Ahmad Malhi</td><td colspan="2">Deputy Manager Finance</td><td>23 Aug, 2023</td></tr>
<tr><td colspan="2">Mr. Muhammad Hassan</td><td colspan="2">Assistant Manager Finance</td><td>23 Aug, 2023</td></tr>
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