RATING REPORT

Engro Powergen Qadirpur Limited

REPORT DATE:
October 24, 2023

RATING ANALYSTS:
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RATING DETAILS				
	Latest Rating		Previous Rating	
Rating Category	**Long-term**	**Short-term**	**Long-term**	**Short-term**
Entity	AA-	A-1	AA-	A-1
Rating Date	*October 24, 2023*		*July 14, 2022*	
Rating Outlook	Positive		Stable	
Rating Action	Maintained		Reaffirmed	

COMPANY INFORMATION	
Incorporated in 2006	**Chairman of the Board:** Mr. Yusuf Jamil Siddiqui
Public Listed Company	**Chief Executive Officer:** Ms. Semeen Akhter
Key Shareholders (with stake 5% or more):	**External Auditors:** A.F. Ferguson & Co, Chartered Accountants
Engro Energy Limited – 68.89%	

APPLICABLE METHODOLOGY(IES)
Applicable Rating Criteria: Corporates (May 2023)
https://docs.vis.com.pk/docs/CorporateMethodology.pdf
VIS Rating Scale
https://docs.vis.com.pk/docs/VISRatingScales.pdf

Engro Powergen Qadirpur Limited (EPQL)

OVERVIEW OF THE INSTITUTION

Engro Powergen Qadirpur Limited is a public listed company, incorporated in Pakistan and its shares are quoted on the Pakistan Stock Exchange Limited. The company is a subsidiary of Engro Energy Limited, which is a wholly owned subsidiary of Engro Corporation Limited. Engro Corporation Limited is a subsidiary of Dawood Hercules Corporation Limited.

Profile of Chairman

Yusuf Siddiqui assumed the role of CEO at Engro Energy Limited on July 1, 2022, following his position as CEO at Engro Vopak and Elengy Terminal Limited since April 2020. With 24 years of experience in the energy industry, he has led ventures in Shell, Eni, and BP, spanning upstream, downstream, and renewables. His global career includes assignments in Tunisia, Jordan, Oman, Netherlands, Iran, Italy, and Pakistan. Mr. Siddiqui holds an engineering degree in Petroleum Engineering from the University of Engineering & Technology, Lahore, and an MBA from the Institute of Business Administration, Karachi. He also serves on the board of Engro Powergen Qadirpur Limited, Engro Energy Services Limited, Engro Energy Limited, Engro Powergen Thar Private Limited, Thar Foundation, Engro

RATING RATIONALE

Engro Powergen Qadirpur Limited ('EPQL' or 'the Company') was incorporated in Pakistan in 2006 as a private limited company. In 2008, the Company was converted to an unlisted public company. EPQL operates a 217.3 Mega-Watt (MW) (net) combined cycle power plant which commenced commercial operations on March 27, 2010. The electricity generated was transmitted to the National Transmission and Dispatch Company (NTDC) under the Power Purchase Agreement (PPA) dated October 26, 2007 which is valid for a period of 25 years from Commercial Operations Date (COD). However in February 2021, after signing of Master Agreement (MA) with the government all NTDC agreements have been novated to Central Power Purchasing Agency (CPPA-G). In 2014, EPQL was listed on Pakistan Stock Exchange (PSX). Engro Corporation Limited (Engro) has majority shareholding in the Company with 68.9% ownership via its wholly owned subsidiary, Engro Energy Limited (EEL). Remaining stake is held by general public and institutions.

The Company has set up a gas based thermal combined cycle power plant near Qadirpur, District Ghotki, Sindh. This is a 1+1+1 configuration plant with one Gas Turbine (GT), one Heat Recovery System Generator (HRSG) and one Steam Turbine (ST). The project converts low British Thermal Unit (BTU), high Sulphur content permeate gas, which was earlier being wasted and flared, into electric power. The plant uses permeate gas as its primary fuel source and High-Speed Diesel (HSD) as the backup fuel. Project cost was funded through a debt-to-equity ratio of 75:25. For debt financing, EPQL obtained foreign currency loan (repaid fully in 2020) from a consortium comprising international financial institutions. A tariff based on a net output of 217.3 MW (permeate gas) and 212.9 MW (HSD) was approved by National Electric Power Regulatory Authority (NEPRA).

Key Rating Drivers

Strong sponsor profile & experienced management team

EPQL is majorly owned (68.9%) by EEL, which itself is a wholly-owned subsidiary of Engro. Engro is a well-established business group with diverse interests and a strong financial foundation. The group operates in various sectors, including fertilizer, dairy, telecom infrastructure, energy & mining, petrochemical, and chemical storage and handling. VIS anticipates that if necessary, the sponsor will provide financial and technical support in the future. The ratings also find reassurance in the substantial experience of EEL/Engro in successfully executing similar projects.

Demand Risk mitigated due to inbuilt take or pay tariff provision and 25-year PPA with power purchaser

The assigned ratings to EPQL consider the Company's low business risk profile, which is supported by the signing of a 25-year long PPA with CPPA-G from COD. Furthermore, the Implementation Agreement (IA) was signed between the Government of Pakistan (GoP) through Private Power and Infrastructure Board (PPIB) and EPQL in 2007. The presence of a long-term PPA with guaranteed capacity payments helps mitigate off-take risk since the power purchaser's obligations are backed by a sovereign guarantee. Additionally, the IA ensures repayment of the Company's receivables in case of default by the power purchaser, with the GoP also paying interest on delayed payments.

Operations & Maintenance Contract: In the past, EPQL had contracted Engro Energy Services Limited (EESL) for its Operations & Maintenance (O&M) services. However, in 2021, EPQL and

Foundation and Gel Nigeria.

EESL reached an agreement on the Termination and Settlement Agreement (TSA). According to the TSA, both parties decided to terminate the O&M Agreement, effective from December 31st, 2021. From January 1st, 2022 onwards, EPQL took on self-operations and maintenance responsibilities.

Gas Supply Agreement (GSA)
The Company has a long-term Gas Supply Agreement (GSA) with Sui Northern Gas Pipelines Limited (SNGPL). The term of this agreement is for a period of 25 years, subject to availability of permeate gas. This contract allows for specific outage allowances for both scheduled and unscheduled outages of the seller and gas producer. Fuel cost is a part of the tariff which mitigates the risk to Company's margins.

Currently, the Company is experiencing gas curtailment from the Qadirpur gas field due to depletion. In response, EPQL has made its plant available on a mixed mode, utilizing both gas and HSD. According to the IA, once the gas curtailment reaches a certain threshold, EPQL is permitted a one-time conversion to an alternate fuel. Meanwhile, while operating on mixed mode, EPQL retains the right to recover full capacity payments. To address the gas depletion issue, the Company has presented a gas depletion mitigation plan (GDMP) to the PPIB, outlining its pursuit of alternate fuel arrangements.

Notably, the Company has secured local gas of 8-13MMSCFD from the Badar gas field operated by Petroleum Exploration Limited (PEL) in 2022. Meanwhile, generation license and tariff modification request has been submitted to NEPRA and the management is engaged actively with the relevant stakeholders to obtain required regulatory approvals. Since the gas field is located only 3KM away from the plant, the associated capex is minimal. Furthermore, the Company is exploring additional options for gas fields in the vicinity. If there is a switch to any alternative fuel, it is anticipated that profitability will remain unaffected, as the fuel cost component will be adapted accordingly. However, its rank in NTDC's economic merit order list might change, potentially impacting dispatch.

Amendment of PPA involving tariff adjustment and recovery of outstanding receivables: On February 11, 2021, the Company and CPPA-G entered into a Master Agreement based on the terms of the MoU, which among other terms included that all undisputed outstanding amounts due and payable to EPQL under the PPA as of November 30, 2020, would be paid in two installments, comprising of cash and government issued securities. Further, the Return on Equity (RoE) and the Return on Equity During Construction (RoEDC) was to be fixed at 17% per annum in PKR (on NEPRA approved equity at Commercial Operation Date) for RoE and RoEDC, calculated at USD/PKR exchange rate of PKR 148/USD, with no future USD indexation. However, the then existing RoE and RoEDC, together with the applicable indexations, were to apply until the date the applicable exchange rate under the then Tariff reached PKR 168/USD and instalments are received by the Company, whereupon the Revised RoE and RoEDC were to become applicable and would apply for the remainder of the term. EPQL received payments against first and second instalment in January 2022 and June 2022, respectively. Consequently, the revised return was applied. Additionally, fuel and operations and maintenance have been considered as single consolidated item and any savings, if determined, from July 1, 2021 will be shared in the ratio of 60:40 between CPPA and Company.

Strong Operational and Financial Performance in 1H'2023 amidst industry challenges.
During 2022, EPQL's electricity generation and delivery to the national grid decreased to 768,202 MWh (2021: 851,197 MWh), resulting in slightly lower revenue recorded at Rs. 10.0b (2021: Rs. 10.2b). The revenue was composed of lower Energy Purchase Price (EPP) payments at Rs. 8.1b (2021: Rs. 8.8b) from combined cycle operations, whereas Capacity Purchased Price (CPP) increased to Rs. 3.1b (2021: Rs. 2.7b) during 2022.

The decrease in sales revenue can be attributed to lower energy dispatch during the year, caused by a scheduled maintenance outage in Q1'2022 for major overhauls, which is performed every six years. The plant's performance has consistently met the normative parameters specified in the PPA. The Company's gross margins increased to 17.1% (2021: 13.6%) during 2022 due to higher capacity payments. EPQL's load factor decreased to 41% in 2022 from 46% in the previous year.

Administrative expenses increased to Rs. 321.1m (2021: Rs. 168.0m) largely due to inflationary adjustments. Despite largely stable delayed payment markup on overdue receivables, net finance income declined to Rs. 135.2m (2021: Rs. 433.5m) owing to higher markup on short-term borrowings and increase in bank charges during 2022. Moreover, as per the IA, the Company is exempt from taxation on its income from the power project, as provided under the Income Tax Ordinance, 2001. However, tax is payable on income from other sources. Therefore, a minimal provision for tax on income from other sources was charged. Resultantly, EPQL's reported net profit of Rs. 1.47b (2021: Rs. 1.59b) during 2022.

During the 1H'2023, the EPQL plant demonstrated a billable availability factor of 100% and a total Net Electrical Output of 496 GWh was delivered to the national grid, with a load factor of 53% compared to the load factor of 36% recorded during the same period in the previous year. The sales revenue during 1H'2023 increased substantially to Rs. 7.1b, compared to Rs. 4.3b in the corresponding period of the previous year. The rise in sales revenue can be primarily attributed to increased EPP payments, which align with higher dispatch volumes. Additionally, a higher Period Weighing Factor (PWF) was applied to CPP payments, leading to better gross margins in 1HY'23. Resultantly, EPQL's profit after tax for 1H'2023 stood at Rs. 1.2b, a notable increase from Rs. 405.6m reported in 1H'2022.

EPQL has maintained its high merit order position on gas. However, with increasing power generation capacity base and with the 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. Nonetheless, in view of cheaper power generation by EPQL vis-à-vis peers, the Company expects to receive dispatch from the power purchaser.

Adequate short-term liquidity amidst circular debt challenges in the energy sector.

The Company maintains a strong liquidity profile, supported by healthy cash flow generation. FFO amounted to Rs. 2.4b while FFO to total debt remained adequate in 2022. The EPQL balance sheet is long-term debt free since 2020, with the Company relying solely on short-term borrowing to meet its working capital requirements. Therefore, the timely recovery of receivables holds significant importance in ensuring short-term liquidity adequacy. In 1H'2023, the FFO for the Company showed significant improvement compared to the same period last year in line with higher profitability. Debt service coverage has remained sizable on a timeline basis.

Nonetheless, the energy sector in the country continues to face challenges due to the growing circular debt, which reached a staggering Rs. 2.6 trillion mark at the end of April 2023. This situation has resulted in liquidity constraints for power producers. In the future, due to the ongoing circular debt issue in the country, it is anticipated that consistent collections from the power purchaser will face continued challenges in the medium term.

Comfortable leverage indicators

During the outgoing year, equity base decreased on account of dividend payout to the tune of Rs. 4.5b. By the end of Jun'23, the total equity of EQPL augmented to Rs. 14.3b (Dec'22: Rs. 13.1b; Dec'21: Rs. 16.2b) as a result of profit retention. The short-term debt carried on the balance sheet decreased to Rs. 4.8b (Dec'22: Rs. 6.0b; Dec'21: Rs. 4.8b) in line with working capital requirements during HY'23. Consequently, as a combined impact of the increase in equity base and lower short-term borrowings as of Jun'23, the gearing and leverage ratios decreased to 0.34x (Dec'22: 0.46x; Dec'21: 0.29x) and 0.78x (Dec'22: 0.84x; Dec'21: 0.70x) respectively.

Corporate Governance and Environmental, Social & Governance (ESF) Framework

EPQL has complied with the requirements of the Listed Companies (Code of Corporate Governance) Regulations, 2019 with total number of 7 directors given in the table below:

Category	*Name*
Independent Director	Mr. Kaiser Bengali
Independent Director (female)	Ms. Nausheen Ahmad
Non-Executive Directors	Mr. Shabbir Hussain Hashmi
	Mr. Vaqar Zakaria
	Mr. Mohammad Yasir Khan
	Mr. Yusuf Jamil Siddiqui (Chairman)
Chief Executive Director	Ms. Semeen Akhter

The meetings of the Board were presided over by the Chairman. The Board has diligently adhered to the stipulations outlined in the relevant Act and Regulations regarding the frequency of meetings, as well as the recording and distribution of minutes from these Board gatherings. In addition to these practices, the Board has also established committees, namely the Board Audit Committee and the Board People Committee i.e. HR and Remuneration Committee.

EPQL remains committed to a comprehensive four-pronged strategy for effectively managing its investments in health, safety, and environmental matters. The Company has formulated a strong strategy tailored to the specific needs and operations of its business. This strategic agenda encompasses the following key aspects: Environmental Footprint Management, Adherence to Local Laws and Global Standards, Occupational Health & Safety and Conservation of Natural Resources.

Over the years, EPQL has effectively balanced its business growth with a diminishing environmental impact, primarily through an eco-efficient approach. The Company's operations hold ISO 14001 certification and maintain full compliance with national environmental regulations. Going beyond mere regulatory compliance, EPQL has adopted rigorous international best practices in environmental management, exemplified by certifications such as the British Safety Council Environmental Program and WWF Green Office certification.

Throughout the year 2022, EPQL meticulously monitored its Environmental Action Plan and the adherence to Social & Environmental covenants. Quarterly reports, as mandated by legal requirements, were consistently submitted to the Sindh Environmental Protection Agency, with no reported deviations from compliance standards throughout the year.

Engro Powergen Qadirpur Limited (EPQL)

FINANCIAL SUMMARY				*(amounts in PKR millions)*
BALANCE SHEET	**Dec'20**	**Dec'21**	**Dec'22**	**Jun'23**
PP&E	12,686	11,815	11,113	10,816
Long term loans and advances	23	14	13	13
Stock in Trade	853	544	844	844
Trade Debts	7,040	11,843	9,800	10,586
Short term investment	49	49	450	50
Advances, Deposits, Prepayments and Other Receivables	4,748	2,872	1,621	1,931
Cash & Bank Balance	13	44	80	1,030
Other Assets	97	263	240	224
Total Assets	**25,510**	**27,445**	**24,162**	**25,494**
Trade & Other Payables	5,191	6,432	4,823	6,015
Accrued Markup	55	61	199	306
Short-term Borrowings	3,618	4,752	6,014	4,826
Long-Term Borrowings *(Inc. current maturity)*	0	0	0	0
Total Debt	3,618	4,752	6,014	4,826
Other Liabilities	1,009	21	20	20
Total Liabilities	9,874	11,267	11,057	11,168
Paid Up Capital	3,238	3,238	3,238	3,238
Total Equity	**15,637**	**16,178**	**13,105**	**14,326**

INCOME STATEMENT	**2020**	**2021**	**2022**	**1H'22**	**1H'23**
Net Sales	8,098	10,204	10,027	4,260	7,080
Gross Profit	1,739	1,383	1,711	426	1,372
Operating Profit	1,649	1,163	1,344	271	1,195
Profit Before Tax	2,094	1,596	1,479	411	1,226
Profit After Tax	2,079	1,594	1,472	406	1,221
FFO	2,646	2,510	2,456	930	1,729

RATIO ANALYSIS	**Dec'20**	**Dec'21**	**Dec'22**	**Jun'23**
Gross Margin (%)	21%	14%	17%	19%
Net Margin (%)	26%	16%	15%	17%
Net Working Capital (Rs. millions)	3,851	4,121	1,771	3,302
FFO to Long-Term Debt (x)	NA	NA	NA	NA
FFO to Total Debt (x)	0.73	0.53	0.41	0.72
Debt Servicing Coverage Ratio (x)	2.32	8.98	6.71	4.78
ROAA (%)	8%	6%	6%	10%
ROAE (%)	14%	10%	12%	18%
Gearing (x)	0.23	0.29	0.46	0.34
Debt Leverage (x)	0.63	0.70	0.84	0.78
Current Ratio (x)	1.43	1.37	1.16	1.30
Inventory + Receivables to Short-term Borrowings (x)	2.18	2.61	1.77	2.37

REGULATORY DISCLOSURES	Appendix II
Name of Rated Entity	Engro Powergen Qadirpur Limited
Sector	Power
Type of Relationship	Solicited
Purpose of Rating	Entity Rating
Rating History	

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
xx/09/2023	AA-	A-1	Positive	Maintained
14/7/2022	AA-	A-1	Stable	Reaffirmed
23/6/2021	AA-	A-1	Stable	Reaffirmed
5/6/2020	AA-	A-1	Stable	Reaffirmed
23/4/2019	AA-	A-1	Stable	Initial

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
1	Anum Irfan	Manager Finance & Planning	August 28, 2023