RATING REPORT

Quaid-e-Azam Thermal Power (Private) Limited

REPORT DATE:
May 24, 2021

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	*24 May'21*		*28 Apr'20*	
Rating Outlook	Stable		Stable	
Rating Action	Reaffirmed		Downgrade	

COMPANY INFORMATION

Incorporated in 2015	**External auditors:** EY Ford Rhodes & Co.
Private Limited Company	**Chairman:** Mr. Abdul Basit **CEO:** Mr. Akhtar Hussain Mayo

Key Shareholders (with stake 5% or more):
- Government of Punjab – 99.99%

APPLICABLE METHODOLOGY(IES)

VIS Entity Rating Criteria: Industrial Corporates (May 2019)
https://www.vis.com.pk/kc-meth.aspx

Quaid-e-Azam Thermal Power (Pvt.) Limited

OVERVIEW OF THE INSTITUTION

Quaid-e-Azam Thermal Power (Private) Limited (QATPL) was incorporated on March 25, 2015 under the companies' ordinance, 1984 (now companies act, 2017).

Profile of Chairman
Mr. Abdul Basit is serving as Chairman of the BoD at QATPL. He is the founder Chairman of Big Bird Group and has previously served as the Chairman Punjab Board of Investment & Trade, Government of the Punjab and president of Lahore Chamber of Commerce and Industries (LCCI) and Chairman of Pakistan Poultry Association (PPA).

Profile of CEO
Mr. Akhtar Hussain Mayo has over 36 years' experience, he is a mechanical engineer by profession. He is currently serving as Chief Executive Officer of QATPL. Previously he served as GM/ Head of Power Plants & Mechanical Section at NESPAK.

RATING RATIONALE

Quaid-e-Azam Thermal Power (Private) Limited (QATPL) is wholly owned by the Government of Punjab (GoPb). The company owns and operates re-liquefied Natural Gas (RLNG) based Combined Cycle Gas Turbine (CCGT) power plant of 1,163 MW generating capacity at Bhikki, District Sheikhupura – Punjab.The ratings draw comfort from the presence of a clause in the Power Purchase Agreement (PPA) whereby QATPL will continue to receive capacity payments during the period of non-supply of gas. In addition, the "Suspension" clause in the PPA allows the company to suspend its plant operations if the receivable amount from Central Power Purchase Agency (Guarantee) Limited (CPPA) at any point in time remains outstanding for 60 days or more, while QATPL will continue to receive capacity payments during the suspension period. This provision further protects the company from the circular debt risk. The plant achieved single cycle commercial operation of Gas Turbines (1 & 2) on June17, 2017. Commercial Operation Date (COD) of combined cycle plant was achieved on May 20, 2018.

The assigned ratings also incorporate subdued sales in FY20 on account of lower off-take, strengthened financial profile as evident from improved profit margins. Albeit, finance cost increased considerably during the outgoing year, bottom-line increased on the back of higher gross margins and other income mainly related to interest income on delayed payments from CPPA-G. Capitalization indicators have improved on a timeline basis owing to re-payments and higher growth in equity base led by profit retention. Cash flow coverages have weakened on a timeline basis on account of sizeable interest charges paid. Corporate governance framework has strengthened given appointment of new independent directors and female representation on board.

Amidst the current pandemic scenario, demand compression for electricity has been observed due to closure of various industries across the country, electricity dispatch is negatively impacted and will likely to persist with the continuation of the economic situation. Moreover, the lower merit order position in the wake of cheaper alternate energy producers also affected QATPL's dispatches. However, capacity payments under PPA are expected to manifest in sustaining company's profitability.

Ratings Drivers

Power Purchase Agreement (PPA): A 30-year PPA was signed between QATPL and Central Power Purchasing Agency (Guarantee) Limited (CPPA-G) on July22, 2016, on behalf of ex-WAPDA Distribution Companies ("the Power Purchaser") for the sale of its entire power generation. Obligations of CPPA are guaranteed by the Government of Pakistan (GoP) under the Implementation Agreement. The PPA covers risk associated with the event of gas non-supply. As per the event, any interruption of supply of gas from and after the Commercial Operations Date (COD) resulting in company's inability to declare full available capacity will be treated as "gas non-supply event" and the company shall continue to receive capacity payments during the non-supply period. Also, QATPL has the right to suspend the supply of available capacity to CPPA after notice if the receivable amount remains outstanding for 60 days or more.

Gas Supply Agreement (GSA): The company has entered into a Gas Supply Agreement (GSA) with Sui Northern Gas Pipeline Limited (SNGPL) on 22 July 2016 for 15 years from Commercial Operations Date (COD). Under this contract, SNGPL will arrange RLNG at the plant site. RLNG fuel price shall be determined by Oil & Gas Regulatory Authority (OGRA) on a periodical basis and any change in the fuel price is a pass-through item under the PPA. Prior to expiry of the GSA, SNGPL shall enter into necessary arrangements to ensure the term is extended for a further period of 15 years for which QATPL shall have the first right of refusal for any gas available in the system.

Sturdy revenue and profits growth supported by higher margins and interest income on delayed payments from CPPA(G)

QATPL delivered 5,192.5 GWh (FY19: 6,147.9GWh) to the national grid, with average annual load factor of 53.91% (FY19 70.50%) during FY20 led by lower off-take due to reduced demand during COVID-19 and availability of cheaper electricity who are positioned better in the merit order. Net revenue was reported lower at Rs. 67.5b (FY19: Rs. 76.9b) during FY20. Cost of sales decreased to Rs. 53.3b (FY19: Rs. 64.4b); around 90% of the total cost is due to consumption of RLNG. QATPL has appointed the joint venture of M/s Harbin

Electric International Company Limited (HEI), China and M/s Habib Rafiq (Pvt.) Limited, (HR) Pakistan, as the Operation and Maintenance (O&M) contractor of the power plant (excluding gas turbines) for a period of 12 years. The company has entered into LTSA with General Electric International Company, Inc. (GE), for twelve years for operation and maintenance of gas turbines, under which the company is committed to pay monthly fee to its LTSA contractor as per terms agreed in the contract. Despite lower electricity deliveries, gross margins improved to 21.1% (FY19: 16.2%), resulting in higher gross profits reported by the company of Rs. 14.2b (FY19: Rs. 12.5b), during FY20. Net sales reported by QATPL during 1HFY21,amounted to Rs. 38.1b vis-à-vis Rs. 37.2b in the corresponding period last year, with 3,856 GWh (1HFY20: 2,702 GWh) energy dispatched by the plant and average annualized load factor of 87.24% (1HFY20: 54.3%). Gross margins have improved during FY20 on account of higher Capacity Purchase Price (CPP) component and lower cost of sales mainly resulting from lower RLNG consumed.

Overall profitability of the company was supported by other income mainly emanating from profit on deposit accounts and interest income on receivables from CPPA-G amounting Rs. 3.7b (FY19: Rs. 2.3m) during FY20. Finance cost stood higher at Rs. 11.2b (FY19: Rs. 8.7b), owing to higher markup rates during FY20. No charge for the review period tax has been recognized, since under relevant clause of Schedule of PPA, corporate income tax payable on generation, sale, exportation or supply of electricity are pass-through items and shall be claimable from CPPA. Based on minimum turnover tax, liability for taxation was Rs. 1b (FY19: Rs. 960.9m) for FY19, and the same has been recorded as claimable from CPPA-G under PPA. The company reported net profit of Rs. 6b (FY19: Rs. 3.3b) during FY20. Given lower finance cost in 1HFY21 led by declining policy rate, net profits stood higher at Rs. 5.2b during 1HFY21 vis-à-vis Rs. 3.1b in 1HFY20. Going forward, on one side profitability of the company is expected to witness a decline on account of ROE reduction notified by NEPRA and on other side if true up decision is announced before 30-June-2021 then it would substantially increase the profitability for the year.

ROE Reduction expected to reduce profits, going forward

In order to compare the returns of GoP owned IPPs and other GoP owned projects, NEPRA has reduced ROE component of the tariff from 16% to 12% but still allowing dollar indexation. The aforementioned has taken effect from October 6, 2020. In lieu of the same, the revised tariff is Rs. 11.3/KWh (Rs. 9.34 EPP component and Rs. 1.97 CPP component) as compared to the initial tariff of Rs. 6.58/KWh. The higher tariff is on account of indexation and fuel price adjustments. Actual impact on profitability can be ascertained after true up decision by NEPRA.

Weakening in liquidity profile underpinned by higher finance costs paid

Liquidity profile of the company has witnessed weakening in FY20 and 1HFY21 on account of sizeable finance charges paid. Funds from Operations (FFO) generated by the company decreased to Rs. 1.1b (FY20: 7.5b; FY19: 9.6b), largely on account of negative difference between incurred and paid finance cost, during 1HFY21. Resultantly, despite reduction in overall borrowings, FFO to total debt declined to 3% (FY20: 11%; FY19: 13%) in 1HFY21. FFO to long-term debt also decreased to 4% (FY20: 13%, FY19: 16%) in 1HFY21. Debt service coverage ratio (DSCR) diminished to 0.77x (FY20: 1.03x; FY19: 1.81x) by end-Dec'20.

Trade receivables increased to Rs. 45.8b (FY20: Rs. 30.3b; FY19: Rs. 24.9b). As per the management, CPPA on average clears the outstanding bills in 50 to 60 days as compared to the regulatory timeframe of 25 days, thereby QATPL earns an interest income on overdue amount at a rate of KIBOR plus 2% per annum.

Receivables from Sui Northern Gas Pipelines Limited (SNGPL) amounted to Rs. 3.3b (FY18: Rs. 3.3b) and represented amount withdrawn from the escrow account by SNGPL in June 2018. For the period from May 2017 to June 2020, SNGPL raised total net invoices of Rs. 11.6b for take-or-pay (the TOP invoices) gas for several months. These invoices were disputed by QATPL, inter alia, on the grounds that (a) take-or-pay, in terms of the GSA, is applicable only on firm gas allocation pertaining to each month which was missing in 2017, (b) the firm gas allocation deliveries plan was not finalized in the year 2018, and (c) the gas not taken by QATPL was diverted and consumed in the same tariff sector in all these years. Pursuant to the dispute resolution mechanism provided for in the GSA, an expert was appointed who rendered his decision which was not acceptable to QATPL as well as SNGPL. Consequently, both QATPL and SNGPL initiated arbitration before London Court of International Arbitration in terms of the dispute resolution mechanism provided for in the GSA. The consolidated arbitration claims are pending and the outcome of the said arbitration will be final and binding upon the parties as prescribed under the GSA. The legal advisors representing QATPL in the arbitration are of the considered view that QATPL has an arguable case. Based on the same the company has not recorded a liability of Rs. 8.4b towards SNGPL and has recorded the remaining amount withdrawn by SNGPL from escrow account, as fully receivable.

Equity base strengthened on back of profit retention

Equity base of QATPL has enhanced on a timeline basis to Rs. 38.7b (FY20: Rs. 33.6b; FY19: Rs. 27.5b) by end-Dec'20 on back of profit retention. Despite consistent debt repayment, total liabilities of the company increased to Rs.97.7b (FY20: Rs. 89.1b; FY19: Rs. 100.9b) at end-Dec'20, mainly due to interim relief liability. During FY20, the company submitted required documents to NEPRA for COD tariff determination. Subsequently, on the request of the company, NEPRA provided provisional indexation adjustment on the reference tariff components of capacity and variable O&M in August'20. In light of the same, QATPL raised invoices for the period from May'18-Dec'20 which resulted in approved interim relief liability of Rs. 18.6b. The rationale for this arrangement was to meet liquidity needs to service debt obligations. Since the aforementioned adjustment is on provisional basis, the company has not recorded the same in revenue.

The company has obtained STFF facility under Common Terms and Accounts Agreement (CTAA) from the consortium of various banks. Principal is repayable in semi-annual installments and carries markup at rate of 3 months KIBOR plus 3%, payable semiannually in arrears; the loan facility will be completely paid-off by end-December 31, 2027.

QATPL has available syndicated working capital facilities of Rs. 11.7b from various banks, carrying markup at rate of 3 months KIBOR plus 1.5%. Accrued markup amounted to Rs. 140m (FY20: 4.6b; FY19: Rs. 4.8b) at end-Dec'20 owing to decline in interest rates and payment of debt repayment installment on its due date i.e. 31-Dec.-20. Trade and other payables decreased to Rs. 15.97b (FY20: Rs. 16.5b; FY19: Rs. 24.1b) mainly due to lower quantum of payables to trade creditors, retention money, and suppliers. The company is liable to pay markup at 1 month KIBOR plus 2% on delayed payment. Gearing decreased slightly to 1.62x (FY20: 2.02x; FY19: 2.62x; FY18: 2.67x) owing to augmentation in equity and debt re-payments.

The Deputy Commissioner Inland Revenue rejected the claim of input tax on construction and installation services and created an additional sales tax demand of Rs. 345.1m for the periods of February' 2017, April-June, 2017. The company has filed an appeal before ATIR which is pending adjudication. Further, the Additional Commissioner (CPRA) issued an order under relevant section of Punjab Sales Tax on Service Act, 2012 (PSTS Act), creating a demand of Rs. 4.9b. The company preferred an appeal before the Commissioner (Appeals) PRA, who issued order rejecting the appeal. The Company, being aggrieved by the order, filed an appeal before ATIR (PRA) on 26-Nov-2019 which is pending adjudication. The company has not recorded any liability in respect of these aforementioned demands on basis of legal and factual grounds.

Corporate Governance: The Board of Directors (BoD) at QATPL consists of 6 independent members. As per corporate governance best practices, present board structure has one female independent director representation. All independent members are experienced professionals from private sector. The financial statements of the company for FY20 were audited by KPMG Taseer&Hadi Co., Chartered Accountants.

Quaid-e-Azam Thermal Power (Private) Limited (QATPL) Annexure I

FINANCIAL SUMMARY *(amounts in PKR millions)*				
BALANCE SHEET	**FY18**	**FY19**	**FY20**	**1HFY21**
PP&E	68,502	64,296	62,422	61,213
Long-Term Deposits & Prepayments	303	4309	4,669	4,669
Stock in Trade	1,658	1631	1,631	1,631
Trade Debts	16,644	24,911	30,035	45,828
Advances, Deposits, Prepayments and Other Receivables	7,575	10,999	11,119	11,992
Cash & Bank Balance	1,286	20,092	10,069	8,255
Other Assets	246	2256	2767	2877
Total Assets	**96,213**	**128,495**	**122,713**	**136,464**
Trade & Other Payables	17,598	24,159	16,543	15,977
Accrued Markup	1,350	4,571	4,810	140
Short-term Borrowings	11,625	11,675	11,675	11,675
Long-Term Borrowings *(Inc. current maturity)*	44,585	60,466	56,120	51,150
Total Debt	56,210	72,141	67,795	62,825
Other Liabilities	8	69	1	18,786
Total Liabilities	75,166	100,939	89,150	97,728
Paid Up Capital	21,250	21,250	21,250	21,250
Total Equity	**21,047**	**27,556**	**33,563**	**38,736**
INCOME STATEMENT	**FY18**	**FY19**	**FY20**	**1HFY21**
Net Sales	10,369	76,868	67,511	38,130
Gross Profit	1,330	12,459	14,213	7,177
Operating Profit	752	12,007	17,249	8,636
Profit Before Tax	-1,225	3,336	6,006	5,173
Profit After Tax	-1,225	3,336	6,006	5,173
FFO	-2,432	9,564	7,528	1,067
RATIO ANALYSIS	**FY18**	**FY19**	**FY20**	**1HFY21**
Gross Margin (%)	13%	16%	21%	19%
Net Margin (%)	-12%	4%	9%	14%
Net Working Capital (Rs. millions)	-6,098	10,118	12,156	13,033
FFO to Long-Term Debt (x)	-5%	16%	13%	4%
FFO to Total Debt (x)	-4%	13%	11%	3%
Debt Servicing Coverage Ratio (x)		1.81	1.03	0.77
ROAA (%)	-1%	3%	5%	8%
ROAE (%)	-6%	14%	20%	29%
Gearing (x)	2.67	2.62	2.02	1.62
Debt Leverage (x)	3.57	3.66	2.66	2.52
Current Ratio (x)	0.82	1.21	1.30	1.24
Inventory + Receivables to Short-term Borrowings (x)	157%	227%	271%	407%

**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	Quaid-e-Azam Thermal Power Private 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
RATING TYPE: ENTITY				
24/05/2021	AA	A-1	Stable	Reaffirmed
28/04/2020	AA	A-1	Stable	Downgrade
04/07/2019	AA	A-1+	Stable	Reaffirmed
04/07/2018	AA	A-1+	Stable	Reaffirmed
19/04/2016	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.
Disclaimer	Information herein was obtained from sources believed to be accurate and reliable; however, VIS does not guarantee the accuracy, adequacy or completeness of any information and is not responsible for any errors or omissions or for the results obtained from the use of such information. VIS is not an NRSRO and its ratings are not NRSRO credit ratings. For conducting this assignment, analyst did not deem necessary to contact external auditors or creditors given the unqualified nature of audited accounts and diversified creditor profile.

Due Diligence Meetings Conducted

	Name	Designation	Date
1	Mr. Salman Shahid	Deputy CFO	April 13, 2021
2	Mr. Imran Farooq	AM Finance	April 13, 2021