RATING REPORT

Quaid-e-Azam Thermal Power (Private) Limited

REPORT DATE:
June 30, 2022

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	*30 Jun'22*		*24 May'21*	
Rating Outlook	Stable		Stable	
Rating Action	Reaffirmed		Reaffirmed	

COMPANY INFORMATION

Incorporated in 2015	**External auditors:** EY Ford Rhodes & Co
Private Limited Company	**Chairman:** Mr. Zaheer Ahmed Ghanghro **CEO:** Mr. Akhtar Hussain Mayo
Key Shareholders (with stake 5% or more): • Government of Punjab – 99.99%	

APPLICABLE METHODOLOGY(IES)

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

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 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 (net) 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. Commercial Operation Date (COD) of combined cycle plant was achieved on May 20, 2018. 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. The Cabinet Committee on Energy (CCoE) approved reduction in capacity charges of Government owned projects in Aug'20 and revised the Return on Equity (ROE) from 16% to 12% with dollar-based indexation. Tariff is expected to be finalized in August'22. The company would recognize the indexation impact on revenue once the true-up decision is made.

During FY21 and HY22, net revenues were reported notably higher on account of higher electricity offtake while the gross margins decreased as a result of lower contribution of CPP component in the revenue mix along with revision in ROE. Overall profitability is supported by interest income on delayed payments from CPPA-G. In addition, lower finance cost in FY21 vis-à-vis preceding years also led to considerable increase in net profits. The equity base has expanded on account of profit retention leading to improvement in capitalization indicators on a timeline basis. Debt service coverage is supported by provisional indexation adjustment on reference tariff provided by NEPRA in the form of interim relief. The company would recognize the actual indexation impact on revenue once the true-up decision is made. The assigned ratings are linked to the continuity of the above arrangements with comfortable debt servicing. The ratings incorporate adequate corporate governance framework underpinned by effective board oversight.

Key Rating 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.

Interest income on delayed payments from CPPA-G continued to support the bottom line: QATPL is high in the merit order list amongst power projects operating on RLNG. During FY21, QATPL delivered 7,119 GWh energy (FY20: 5,193 GWh) to the national grid, with higher average annual load factor of 77% (FY20: 54%). Accordingly, net sales were reported higher at Rs. 78.9b (FY20: Rs. 67.5b) mainly in line with increase in EPP component. Cost of sales increased to Rs. 65.2b (FY20: Rs. 53.3b); around 90% of the cost of sales constituted RLNG consumed. Gross margins decreased to 17.4% (FY20: 21.1%) on account of lower proportion of Capacity Purchase Price (CPP) component along with revision in Return on Equity (ROE) from 16% to 12% in Aug'20. In order to compare the returns of government owned IPPs and other power projects, NEPRA has reduced ROE component of the tariff with dollar indexation.

Other expenses largely comprised markup on delayed payments to SNGPL and O&M contractor while increase in other expenses during FY21 and HY22 is primarily related to workers fund contributions and provision for corporate social responsibility. Overall profitability of the company was supported by other income (HY22: Rs. 2.0b; FY21: Rs. 3.6b; FY20: Rs. 3.7b) mainly emanating from interest income on receivables from CPPA-G and profit on deposit accounts. In addition, during FY21, finance cost decreased considerably to Rs. 6.7b (FY20: Rs. 11.2b) in line with lower average markup. Based on alternative corporate tax, liability for taxation was Rs. 1.8b (FY20: Rs. 1.0b) for FY21, and the same has been recognized as claimable from CPPA-G under PPA, 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. However, income tax on few items of other income is not recoverable from CPPA-G, hence tax amounting Rs. 341.9m was charged in the outgoing year. Net profits augmented to Rs. 9.2b (FY20: Rs. 6.0b) in FY21.

During HY22, net sales were reported notably higher at Rs. 61.4b vis-à-vis Rs. 38.2b in the preceding period last year on account of higher average energy prices while power offtake was lower at 3,361 GWh (HY21: 3,857 GWh) with a load factor of 72% (HY21: 87%). Gross profit increased modestly to Rs. 7.4b (HY22: Rs. 7.2b) while gross margin declined to 12.1% in HY22. Net profit stood at Rs. 5.3b (HY21: Rs. 5.2b) in HY22.

Debt service coverage is supported by provisional indexation adjustment on reference tariff in form of interim relief: The company generated Rs. 8.4b in Funds from operations (FFO) (FY20: Rs. 7.5b) in line with higher profitability. Resultantly, FFO to total debt and FFO to long-term debt increased to 0.13x (FY20: 0.11x) and 0.16x (FY20: 0.13x). Debt service coverage ratio (DSCR) improved slightly to 1.25x (FY20: 1.19x). Meanwhile, in HY22, FFO decreased to Rs. 3.0b mainly on account of negative difference between incurred and paid finance cost. Annualized FFO to total debt and long-term debt decreased slightly while DSCR declined to 0.78x largely due to higher long-term repayments (HY22: Rs. 5.5b; FY21: Rs. 5.0b; FY20: Rs. 4.6b) in HY22. Meanwhile, debt servicing is supported by an arrangement provided by NEPRA, which entails provisional indexation adjustment on the reference tariff components of capacity and variable O&M. The company has reported interim relief of Rs. 3.3b (FY21: Rs. 20.9b; FY20: Nil) in HY22 cash flows; accounting for the same, the debt service coverage exceeds 1.0x during HY22 (FY21: 2.80x). The actual interim relief liability would be higher than the annualized amount of Rs. 6.7b due to the impact of dollar indexation and KIBOR in 2HY22. However, incorporating the same annualized amount of interim relief liability in FFO, adjusted DSCR comes out to be 1.21x for FY22.

Trade receivables from CPPA-G increased to Rs. 66.8b (FY21: Rs. 57.3b; FY20: Rs. 30.3b) by end-HY22. These receivables are interest free and secured by guarantee from the GoP under the Implementation Agreement. However, a penal markup at the rate of 3 months KIBOR plus 2% is charged, in case the amount is not paid within due date. 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 the overdue amount. These receivables also include delayed payment interest amounting to Rs. 7.1b (FY21: Rs. 5.4b; FY20: Rs. 3.5b) and receivables on disputed invoices from CPPA-G amounting to Rs. 4.3b (FY21: Rs. 3.4b; FY20: Rs. 2.2b) at end-HY22. Sales tax refundable stood at Rs. 3.2b (FY21: Rs. 3.4b; FY20: Rs. 3.6b), including amount of Rs. 986.1m against which the company has filed an appeal before Honorable High Court to recover as input tax claim. In addition, the company has also recorded Rs. 1.1b, recoverable from FBR on the basis of legal and factual grounds.

Receivables from SNGPL amounted to Rs. 3.3b (FY21 & FY20: Rs. 3.3b) and represented amount withdrawn from the escrow account by SNGPL in June 2018. During the current and previous years, SNGPL raised total net invoices of Rs. 12.9b (FY21: Rs. 12.5b; FY20: Rs. 11.6b) for take-or-pay (the TOP invoices) gas for several months from May 2017 to December 2021. 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. 12.9b towards SNGPL and has recorded the remaining amount withdrawn by SNGPL from escrow account, as fully receivable.

Equity base strengthened on the back of profit retention: Equity base of QATPL augmented to Rs. 48.0b (FY21: Rs. 42.7b; FY20: Rs. 33.6b) by end-Dec'21 due to internal capital generation. Total liabilities stood higher at Rs. 106.4b (FY21: Rs. 103.1b; FY20: Rs. 89.2b) at end-HY22. Significant increase in total liabilities at end-FY21 and HY22, is primarily due to recording interim relief liability amounting Rs. 24.3b (FY21: Rs. 20.9b; FY20: Nil) as at Dec 31, 2021, related to provisional indexation impact.

The company has obtained STFF facility under Common Terms and Accounts Agreement (CTAA) from the consortium of 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 retired by end-December 31, 2027. In addition, QATPL has availed syndicated working capital facilities of Rs. 15.7b (FY21 & FY20: 11.7b) from various banks, carrying markup at rate of 3 months KIBOR plus 1.5%. Accrued markup amounted to Rs. 366.7m (FY21: Rs. 2.9b; FY20: 4.6b) at end-Dec'21. Trade and other payables increased to Rs. 20.2b (FY21: Rs. 16.1b; FY20: Rs. 16.5b) mainly due to higher payables to trade creditors and suppliers. The company is liable to pay markup at 1-month KIBOR plus 2% on delayed payments. Gearing was reported lower at 1.28x (FY21: 1.47x; FY20: 2.02x) on the back of equity expansion and debt repayments.

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 Nov 26, 2019, which is pending adjudication. The company has not recorded any liability in respect of these demands on basis of legal and factual grounds.

Corporate Governance: Presently, the Board of Directors (BoD) at QATPL consists of thirteen members including Chairman, CEO, eight independent members and three ex-officio members. The Ex-Officio members (nominee personnel of GoPb) included Secretary Energy, Chairman Planning & Development and Secretary Finance. The financial statements of the company for FY21 were audited by EY Ford Rhodes, Chartered Accountants, who have been reappointed for FY22. The composition of BoD is tabulated below:

Directors	Status
Mr. Zaheer Ahmed Ghangro	Chairman
Mr. Akhtar Hussain Mayo	Chief Executive Officer
Mr. Muhammad Ajmal Bhatti (Secretary Energy)	Ex-Officio Director
Mr. Ali Sarfaraz Hussain (Chairman P&D, GoPb)	Ex-Officio Director
Mr. Iftikhar Amjad (Secretary Finance)	Ex-Officio Director
Ms. Aasia Saail Khan	Independent Director
Mr. Khurram Saleem	Independent Director
Mr. Naweed Akhtar Sharif	Independent Director
Mr. Tariq Mehmood	Independent Director
Mr. Muhammad Ali	Independent Director
Mr. Farrukh Ifzal	Independent Director
Mr. Waseem Akhtar	Independent Director

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

FINANCIAL SUMMARY *(amounts in PKR millions)*			
BALANCE SHEET	**FY20**	**FY21**	**HY22**
PP&E	62,422	60,032	58,914
Long-Term Deposits & Prepayments	4,669	4,669	7,354
Stock in Trade	1,631	1,508	807
Trade Debts	30,035	57,342	66,847
Advances, Deposits, Prepayments and Other Receivables	11,119	9,931	10,687
Cash & Bank Balance	10,069	9,372	6,863
Total Assets	**122,713**	**145,801**	**154,415**
Trade & Other Payables	16,543	16,068	20,193
Accrued Markup	4,810	2,939	367
Short-term Borrowings	11,675	11,675	15,675
Long-Term Borrowings ***(Inc. current maturity)***	56,120	51,212	45,757
Total Debt	67,795	62,887	61,432
Other Liabilities	1	21,178	24,407
Total Liabilities	**89,150**	**103,072**	**106,399**
Paid Up Capital	21,250	21,250	21,250
Total Equity	**33,563**	**42,729**	**48,016**
INCOME STATEMENT	**FY20**	**FY21**	**HY22**
Net Sales	67,511	78,935	61,446
Gross Profit	14,213	13,747	7,404
Operating Profit	17,249	16,249	8,704
Profit Before Tax	6,006	9,512	5,286
Profit After Tax	6,006	9,170	5,286
FFO	7,528	8,367	2,992
RATIO ANALYSIS	**FY20**	**FY21**	**HY22**
Gross Margin (%)	21.1	17.4	12.0
Net Margin (%)	8.9	11.6	8.6
Net Working Capital (Rs. millions)	12,157	17,818	15,695
FFO to Long-Term Debt (x)	0.13	0.16	0.13*
FFO to Total Debt (x)	0.11	0.13	0.10*
Debt Servicing Coverage Ratio (x)	1.19	1.25	0.78
ROAA (%)	4.8	6.8	7.0*
ROAE (%)	19.7	24.0	23.3*
Gearing (x)	2.02	1.47	1.28
Debt Leverage (x)	2.66	2.41	2.22
Current Ratio (x)	1.30	1.30	1.23
Inventory + Receivables to Short-term Borrowings (x)	2.71	5.04	4.32

**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 Ratings
Rating History	

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
RATING TYPE: ENTITY				
30/06/2022	AA	A-1	Stable	Reaffirmed
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.
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Due Diligence Meetings Conducted		Name	Designation	Date
	1	Mr. Salman Shahid	Deputy CFO	May 30, 2022