RATING REPORT

Neelum Jhelum Hydropower Company (Private) Limited

REPORT DATE:
June 28, 2016

RATING ANALYSTS:
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RATING DETAILS

	Final Rating	Preliminary Rating
Rating Category		
Sukuk	AAA	AAA
Rating Date	*June'28, 2016*	*April'12, 2016*
Rating Outlook	Stable	Stable

COMPANY INFORMATION

Incorporated on November 18th, 2004	External auditors: Ernst & Young Ford Rhodes Sidat Hyder
Private Limited Company	Chairman of the Board: Mr. Zafar Mahmood
Key Shareholders (with stake 5% or more):	Chief Executive Officer: Lt. Gen. Muhammad Zubair (Retd.)
WAPDA (Water & Power Development Authority) – 99%	

APPLICABLE METHODOLOGY(IES)

JCR-VIS Entity Rating Criteria: Industrial Corporates (October 2003)
http://jcrvis.com.pk/images/IndustrialCorp.pdf

Rating The Issue (September 2014)
http://jcrvis.com.pk/Images/criteria_instrument.pdf

Neelum Jhelum Hydropower Company (Private) Limited

OVERVIEW OF THE INSTITUTION

Neelum Jhelum Hydropower Company (Private) Limited (NJHPC) was incorporated on 18th November 2004. The company is a Special Purpose Vehicle (SPV) constituted as a subsidiary of WAPDA (Water and Power Development Authority) for the generation and sale of electricity via the development of Neelum Jhelum Hydropower Power (NJHPP) project.

WAPDA, the parent entity, has a hydel generation capacity of 6,902MW with a plant utilization factor of 52.6%. The company reported net profit of Rs. 33.7b during FY15 while equity base was reported at Rs. 184.2b at end-FY15.

RATING RATIONALE

The assigned rating to the Rs. 100b Sukuk issue incorporate unconditional and irrevocable first demand guarantee issued by the President Islamic Republic of Pakistan (on behalf of the Government of the Islamic Republic of Pakistan) (GoP) covering issue amount of the Sukuk alongwith profit payments. GoP would pay the entire called amount immediately upon receiving a demand notice from the trustee. Ratings also reflect financial strength and demonstrated support from the parent entity, Water and Power Development Authority, in the form of equity injection and funding support.

The demand for electricity in Pakistan exceeds supply by over 5,000 MW and peak shortfall extends up to around 8,000MW.As per the energy planning expert group of China-Pakistan Economic Corridor (CPEC), annual growth rate of electricity demand is projected to grow at 7.8% resulting in an increase in shortfall to over 10,000MW. Hydropower generation, currently contributing less than one-third of the total power generation, is one of the important sources envisioned by the government in order to bridge this shortfall. As per Private Power and Infrastructure Board, hydropower generation in the country has a potential of 60,000MW with Pakistan currently utilizing slightly over one-tenth of the same.

NJHPC was setup to design, construct, own, operate and maintain Neelum Jhelum Hydropower Project (NJHPP); a 969MW run-of-the-river project in Azad Jammu & Kashmir. NJHPP will add around 5% to the country's total installed power generation capacity and will be the 4th largest hydropower project in the country representing 12% of total installed hydel capacity. The project is based on a perennial river system and the supply of water has been determined to be adequate, given the water treaty arrangements. Moreover, hydrological risk is to be borne by the power purchaser as per power policy. Given that NJHPP is an early riser it would provide substantial power generation from April to June, replacing expensive thermal generation, when Tarbela power station will be running at minimum power capacity. Annual electricity generation is expected at 5.15billion units at average 59.4% capacity utilization. As per management, impact of construction of Kishanganga Hydropower on power generation would be limited as almost three fourth of the water is contributed by local tributaries to Neelum at Nauseri while India has to release a specified quantity of water (9 cumecs) as per ruling by International Court of Arbitration.

As per the revised PC-1 2015, the total project cost is estimated at Rs. 404billion with the project having faced several delays and cost overruns. The major reason for variation was on account of consultants being engaged for the project in 2008, who reviewed the entire design of the project and recommended numerous changes in design on the basis of new seismic parameters dictated by earthquake in 2005. Other reasons include change in price level, additional consultancy cost, higher exchange loss & duties, shifting of power house and dam location. As of February'2016, the project has achieved 80% physical completion. Around three fourth of the total cost is being funded through debt while the remaining portion will be funded through equity. Given the shortage of funding, we have noted that a portion of Interest during Construction (IDC) to the tune of Rs. 18.7b has been deferred. Moreover, IDC for NBP Sukuk has not been built in the project cost and around Rs. 12.5b has been set aside from the loan itself for this purpose. The first generating unit of the project in expected to start production by mid-2017 and the rest of the three units are planned to come online in a phased manner by December'2017. Timely completion of the project is considered important given that debt payments for the Sukuk commence from 2018. The management intends to shortlist consultant shortly for drafting of power purchase agreement and finalization of tariff.

The planned Sukuk will be unlisted, privately placed having a tenor of 10 years inclusive of a grace period of 2 years. Sukuk will have semi-annual principal and rental payments and draw down is planned in three tranches. Apart from GoP guarantee, security structure of the Sukuk entails charge on all unencumbered present and future assets of the company and exclusive lien over debt payment account (DPA). As per the waterfall mechanism, an amount equivalent to one-sixth of the installment amount will be deposited each month so that DPA on the installment date is equivalent to the installment amount. In case of any shortfall in DPA Account by NJHPC, WAPDA will inject the required funds. As per management, financial viability is supported by the tariff mechanism for hydropower projects which is based on cost plus return on investment. Approval of envisioned tariff is considered important for standalone financial profile of the institution and for adequate debt servicing. Moreover, timely payment from the power purchaser will also remain an important rating factor.

ISSUE/ISSUER RATING SCALE & DEFINITIONS — Appendix IV

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: JCR-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.jcrvis.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.jcrvis.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.

'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.jcrvis.com.pk/images/policy_ratings.pdf

'SD' Rating: An 'SD' rating is assigned when JCR-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 V

Name of Rated Entity	Neelum Jhelum Hydropower Company (Private) Limited
Sector	Power
Type of Relationship	Solicited
Purpose of Rating	Sukuk rating
Rating History	
Instrument Structure	Apart from GoP guarantee, security structure of the Rs. 100billion Sukuk entails charge on all unencumbered present and future assets of the company and exclusive lien over debt payment account (DPA). As per the waterfall mechanism, an amount equivalent to one-sixth of the installment amount will be deposited each month so that DPA on the installment date is equivalent to the installment amount. In case of any shortfall in DPA Account by NJHPC, WAPDA will inject the required funds.
Statement by the Rating Team	JCR-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.
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Rating History:

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
RATING TYPE: ENTITY				
28/06/2016	AAA	N/a	Stable	Final
12/04/2016	AAA	N/a	Stable	Preliminary