RATING REPORT

Neelum Jhelum Hydropower Company (Private) Limited

REPORT DATE:
January 12, 2023

RATING ANALYSTS:
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RATING DETAILS		
	Instrument Rating	
Rating Category	Latest Rating	Previous Rating
Sukuk	AAA	AAA
Rating Date	*Jan 12, 2023*	*Jan 12, 2022*
Rating Outlook	Stable	Stable
Rating Action	Reaffirmed	Reaffirmed

COMPANY INFORMATION	
Incorporated in 2004	**External auditors:** BDO Ebrahim & Co. Chartered Accountants
Private Limited Company	**Chairman:** Lt. Gen (Retd) Sajjad Ghani **CEO:** Mr. Muhammad Arfan
Key Shareholders (with stake 5% or more):	
Water & Power Development Authority (WAPDA) – 100%	

APPLICABLE METHODOLOGY(IES)
VIS Entity Rating Criteria: Corporates (August 2021) **Rating the Issue (November 2021)** *https://docs.vis.com.pk/docs/CorporateMethodology202108.pdf* *https://docs.vis.com.pk/docs/Notchingtheissue202007nov.pdf*

Neelum Jhelum Hydropower Company (Private) Limited

OVERVIEW OF THE INSTITUTION	RATING RATIONALE
Neelum Jhelum Hydropower Company (Private) Limited (NJHPC) was incorporated on November 18, 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 project (NJHPP).	Neelum Jhelym Hydroelectic project is a mega project that carries immense national importance. It is located in the vicinity of Muzaffarabad, Azad Jammu & Kashmir. The project diverts Neelum river water through tunnels at Nauseri about 41km upstream of Muzaffarabad and out falling in Jhelum river at Zaminabad near Chattar Kalas. Powerhouse is located 22km downstream of Muzaffarabad at Chattar Kalas.

The rating assigned to the Sukuk issue take into account 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 along with profit payments. GoP would immediately pay the entire called amount once the demand notice from the trustee is received. Ratings also incorporate strong financial muscle and implicit support from the parent entity, Water and Power Development Authority (WAPDA), in the form of equity injection and funding support.

The company signed an interim PPA with CPPA-G on January 8, 2020, which was valid for one year effective from revised tariff notification dated October 17, 2019, and was extendable with mutual consent of all parties. Subsequent to the lapse of one year ended on October 16, 2020, the management did not opt for extension of interim PPA, as a petition was filed regarding final tariff with CPPA-G in November'2020. CPPA-G forwarded Company's request to NEPRA in February 2021. The public hearing was held on June 21, 2021 at NEPRA Head office; however, the tariff petition could not proceed on its merits due to the absence of third-party validation of project costs. Resultantly, the interim tariff of Rs. 9.1184 per kWh has been extended on **take and pay basis with must run condition** until the company gets waiver of third-party validation requirement or conducts the validation. After complying with either of the two condition, the company will file a final tariff petition through CPPA-G.

Physical progress stands at 99.96% and taking over certificate for whole of the works was signed and issued on December 21, 2021. However, the plant was shut down on July 03, 2022 due to an unforeseen incident at the Tailrace tunnel.

NJHPC was setup to design, construct, own, operate and maintain Neelum Jhelum Hydropower Power Project (NJHPP) which is a state-of-the-art, world class underground facility with installed capacity of 969 MW (4 Turbines of 242.25 MW each). The main purpose is the development of NJHPP for generation and sale of electricity to CPPA-G. It is a Composite Dam (Gravity + Rock fill) having height of 60 meters, with a tunnel system comprising Twin Tunnels (19.60 km each), Single Tunnel (8.94 km) and Tailrace Tunnel (3.55 km). All four units remained operational during FY22; however, given generation capacity of the power plant is directly linked to the availability of water there is sizeable seasonal variation in energy generation. Since commissioning, the project has generated energy of **18,178.6 million kWh** up to June 30, 2022.

As per the latest progress report dated July 06, 2022, physical progress stood at 99.96% at end-June'22. Taking over certificate of the whole of the works of the project was signed and issued to the contractor on December 21, 2021. Financial progress (with Interest During Construction (IDC) etc.) stood at 82.49% at end-June'2022.

As per the 4th revision in PC-1 2017, the approved contract cost was Rs. 506.8b; however, as per management, the project is completed within Rs. 428b. Accounting for IDCs and other costs, total expenditure amounted to Rs. 418.1b as per the latest progress report. The project cost is being funded through a debt: equity: grant ratio of 74:10:16, with grant component covered by the Neelum Jhelum Surcharge (NJS).

Impact of plant closure on Sukuk repayments

VIS has been informed that the project has been shut on July 04, 2022 due to an unforeseen incident at Tailrace Tunnel. The inspection of the damaged area has been done and the recovery activities are underway that are expected to be resolved **by June'23**, as per management. Further, according to management, debt servicing during the tenure of the shutdown will be arranged though monthly receipt of outstanding receivables from Central Power Purchasing Agency (CPPA-G). The trustee has confirmed collection of up to date principal and interest payments in the Debt Payment Account (DPA). Through the receipt of the receivables, the company successfully paid the due principal amount at end-Dec'22. VIS will continue to track the balance of DPA on a monthly basis. Any shortfall in the same during any month may warrant revision in ratings.

The company expects final tariff to vary from the provisional tariff notified by NEPRA

Under the interim PPA, the company is obligated to sell and deliver all output of the plant on 'take and pay' basis at the tariff notified by NEPRA. The revised provisional tariff of Rs. 9.1184/kWh, announced on August 19, 2019, included components of debt repayment and Operations & Maintenance (O&M) is still applicable; meanwhile, the components of insurance, water use surcharge and profitability will be added once the final tariff is decided. The levelized final tariff for 30 years is expected to be Rs. 10.3/kWh that would be implemented upon the waiver or completion of third-party validation, and signing of financial PPA.

With the power complex operating as per availability of water in FY22, revenue to the tune of Rs. 43.6b (FY21: Rs. 44.8b) was recorded. Reduction in the same was a function of lower generation albeit late payment surcharge from CPPA-G increased in the review period. Net trade debts (excluding provision against delayed payment charges at 3MK+2%) from CPPA-G mounted to Rs. 82.9b (FY21: Rs. 52.1b) at end-June'22. Aging depicts that around 76% of the gross trade debts are due over 120 days. Receiving escalated receivables amidst subdued macroeconomic environment will be important.

Bottom-line reduced largely due to higher tax charge from previous years on income from the profits earned from income other than sale of electricity.

Revenue of the company is exempt from sales tax for a period of five years from the date of commencement of commercial production under notification issued by Azad Jammu and Kashmir Central Board of Revenue. The company reported lower gross profit of Rs. 31.8b (FY21: Rs. 33.2b), which translated into gross margin of 73% (FY21: 74%). During FY22, the company also recorded provision against delayed payment charges due from CPPA-G to the tune of Rs. 3.7b (FY21: Rs.

2.2b). Finance cost declined to Rs. 23.8b (FY21: Rs. 25.6b) mainly due to lower quantum of borrowings. Other income increased due to higher interest income on bank accounts. The company reported lower net profit after tax to the tune of Rs. 402.8m (FY21: Rs. 3.5b) during FY22 due to higher tax charge from previous years (2009-2018) on income other than sale of electricity.

In line with lower profits, Funds from Operations (FFO) decreased to Rs. 22.3b (FY21: Rs. 27.4b). The debt service coverage ratio (excluding Foreign Relent Loans and Cash Development Loans from GoP on which the company defaulted) was recorded lower at 1.35x (FY21: 1.48x) at end-June'22. During the outgoing year, the company made an additional balloon debt repayment with a cumulative principal repayment of Rs. 20.5b against due amount of Rs. 12.5b.

Capitalization

Overall equity base increased to Rs. 106.3b (FY21: Rs. 105.9b) as the retention of profits led to decrease in accumulation losses to Rs. 9.9b (FY21: Rs. 10.3b) by end-FY22. Equity contribution by GoP in the form of NJS amounted to Rs. 69.3b (FY20: Rs. 69.3b), which was collected from electricity consumers of distribution companies (DISCOs) operating in Pakistan.

Long-term financing from financial institutions through GoP (including current maturity) stood 168.8b (FY21: Rs. 170.5b). Short-term borrowings from WAPDA decreased to Rs. 10b (FY21: Rs. 11.0b) on account of payment settlement during the year; these borrowings represent amount payable to WAPDA on account of principal and interest payments made by WAPDA of various foreign relent and local loans on behalf of the company. Increase in accrued markup payable was due to delay repayment of FRL and CDL loans. The external auditors have reclassified long-term financing as current liabilities owing to default in payments of principal and interest amounts to the GoP. Diminishing musharaka repayments are being made on time while delay in long-term financing repayments is due to non-finalization of tariff and delays in payments from CPPA-G against the sale of electricity. The company is negotiating a revised repayment schedule for its long-term (excluding diminishing musharaka) and short-term loans that would be aligned with the company's revenue stream under its final tariff and PPA.

The Sukuk certificates carry profit at a rate of 6-month KIBOR Plus 1.75% with semiannual rental payments. NJHPP is entitled to a rebate (Hiba) of up to 0.62% in case the installments (rental + principal) are made within 30 days of the due date. Ratings of the Sukuk draws comfort from presence of a Debt Payment Accounts which follows a waterfall mechanism. As per the waterfall mechanism, an amount equivalent to one-sixth of the installment amount is being deposited each month so that debt payment account (DPA) on the installment date is equivalent to the installment amount. In case of any shortfall in DPA by NJHPC, WAPDA will inject the required funds. In the absence of any income stream, DPA would be recharged with the borrowed amount. As per the management, DPA has been filled with the required amount to be paid on the due date with monthly payments received against invoices from CPPA-G. Redemption schedule of the outstanding Sukuk is tabulated below which shows the balloon payment made in FY22:

Rs. In b

	Principal Outstanding	Payment Date	Principal payment	Interest Payment	Total Dues
	100.00	28.12.2018	6.25	4.09	10.34
	93.75	28.06.2019	6.25	5.57	11.82
Actual	87.50	28.12.2019	6.25	6.25	12.50
	81.25	28.06.2020	6.25	5.94	12.19
	75.00	28.12.2020	6.25	3.13	9.38

	68.75	28.06.2021	6.25	2.91	9.16
	62.50	28.12.2021	6.25	2.76	9.01
	56.25	28.06.2022	14.25	3.42	17.67
	42.00	28.12.2022	5.25	3.46	8.71
	36.75	28.06.2023	5.25	3.45	8.70
	31.50	28.12.2023	5.25	2.97	8.22
	26.25	28.06.2024	5.25	2.46	7.71
Projected	21.00	28.06.2024	5.25	1.98	7.23
	15.75	28.06.2025	5.25	1.48	6.73
	10.50	28.12.2025	5.25	0.99	6.24
	5.25	28.06.2026	5.25	0.49	5.74

Neelum Jhelum Hydropower Company Annexure I

FINANCIAL SUMMARY *(amounts in PKR millions)*				
BALANCE SHEET	**FY19**	**FY20**	**FY21**	**FY22**
Operating Fixed Assets	404,317	390,761	381,786	374,878
Long-term Advances	336	301	301	301
Trade Debts	-	68,645	52,152	82,913
Contract Assets	36,147	932	27173	0
Other Assets	552	388	483	784
Bank Balances	38,231	23,992	23,656	16,546
Total Assets	**479,583**	**485,019**	**485,560**	**475,422**
Long-Term Financing *(Inc. current maturity)*	169,034	171,088	170,522	168,781
NBP Sukuk *(Inc. current maturity)*	87,500	75,000	65,500	42,000
Trade and Other Payables	21,073	17,068	22,060	27,516
Short-term Borrowings	16,048	15,048	11,000	10,000
Accrued Markup	80,068	95,439	104,373	112,678
Other Liabilities	7,726	8,878	6,161	8,100
Total Liabilities	**381,448**	**382,532**	**379,616**	**369,075**
Issued Capital	41,664	41,664	41,664	41,663
Accumulated (Loss)/Profit	-14,445	-13,783	-10,325	-9,923
Share Deposit Money	5,300	5,300	5,300	5,300
Government Grant	65,616	69,307	69,307	69,307
Total Equity	**98,135**	**102,487**	**105,945**	**106,348**
INCOME STATEMENT	**FY19**	**FY20**	**FY21**	**FY22**
Net Revenue	27,798	45,262	44,826	43,619
Gross Profit	18,764	35,111	33,206	31,827
Finance Cost	30,355	33,178	25,588	23,783
Other Income	3,596	3,296	1,944	2,580
Profit/(Loss) Before Tax	-9,562	1,615	4,010	2,836
Profit/(Loss) After Tax	-8,200	1,615	3,458	403
FFO	-	31,815	27,511	22,304
RATIO ANALYSIS	**FY19**	**FY20**	**FY21**	**FY22**
Gross Margin (%)	68%	78%	74%	73%
Net Margin (%)	-	4%	8%	1%
FFO to Long-Term Debt (x)	-	13%	16%	13%
FFO to Total Debt (x)	-	12%	11%	9%
Debt Servicing Coverage Ratio (x) [For commerical bank obligations]	-	1.64	1.49	1.00
Gearing (x)	2.78	2.55	2.33	2.08
Debt Leverage (x)	3.89	3.73	3.58	3.47
Current Ratio (x)	0.2	0.25	0.28	0.30

ISSUE/ISSUER RATING SCALE & DEFINITIONS Annexure 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	Annexure III
Name of Rated Entity	Neelum Jhelum Hydropower Company
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				
January 12, 2022	AAA		Stable	Reaffirmed
September 19, 2022				Note
January 12, 2022	AAA		Stable	Reaffirmed
December 30, 2020	AAA		Stable	Reaffirmed
December 24, 2019	AAA		Stable	Reaffirmed
January 02, 2019	AAA		Stable	Reaffirmed
September 13, 2017	AAA		Stable	Reaffirmed
April 12, 2016	AAA		Stable	Reaffirmed

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
Mr. Mudassar Shehzad	Manager Accounts & Finance	January 03, 2023