RATING REPORT

Superhighway Construction Operation & Rehabilitation Engineering (Private) Ltd. (SCORE)

REPORT DATE:
02nd April, 2021

RATING ANALYSTS:
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RATING DETAILS		
Rating Category	**Latest Rating**	**Previous Rating**
Entity	AA-/A-1	AA-/A-1
Rating Date	*April'02, 2021*	*October'30, 2019*
Rating Outlook	Stable	Stable

COMPANY INFORMATION	
Incorporated on February 27, 2015.	**External auditors**: KPMG Taseer Hadi & Co.
Private Limited Company	**Chairman of the Board:** Maj. Gen. Kamal Azfar
Key Shareholders (with stake 5% or more):	**Chief Executive Officer**: Brig. Waqar Hafeez Abbasi
Frontier Works Organization – 100%	

APPLICABLE METHODOLOGY(IES)

VIS Entity Rating Criteria: Toll Roads (August 2020)
https://s3-us-west-2.amazonaws.com/backupsqlvis/docs/TollRoads202008.pdf

VIS Entity Rating Criteria: Industrial Corporates (April 2019)
https://s3-us-west-2.amazonaws.com/backupsqlvis/docs/Corporate-Methodology-201904.pdf

Superhighway Construction Operation & Rehabilitation Engineering (Private) Ltd. (SCORE)

PROFILE

Superhighway Construction Operation and Rehabilitation Engineering (Pvt.) Limited (SCORE) was incorporated in February, 2015 under the companies ordinance, 1984.

FWO was incorporated in 1966, by the Engineering Corps of Pakistan Army for the construction of Karakoram Highway.

RATING RATIONALE

Superhighway Construction Operation and Rehabilitation Engineering (Pvt.) Limited (SCORE) is a Special Purpose Vehicle (SPV), a wholly-owned subsidiary of Frontier Works Organization (FWO). FWO is an autonomous organization which has played a key role in the development of bridges, roads, tunnels, airfield and dams in Pakistan.

SCORE was incorporated for the conversion of existing 4-lane Karachi-Hyderabad Superhighway into a 6 lane (M-9) road. The project is based on build, operate and transfer basis. SCORE has entered into a 25-year concession agreement with National Highway Authority (NHA) starting in March 2015. Furthermore, SCORE has also signed an Operations and Maintenance (O&M) contract with Frontier Works Organization (FWO). FWO was also involved in the construction of the road and has provided an unconditional guarantee for debt repayment in favour of SCORE.

M-9 is a 136 kilometers motorway from Karachi to Hyderabad with 10 interchanges. Project deliverables also include construction of 275 km long service road (TST), 2 Motorway Service Areas (MSA), 11 bridges, electronic toll collection system and fencing of Motorway (leaving the urbanized area). The motorway has been almost entirely been completed in terms of percentage of work done (The company received substantial completion certificate from the Quality Assurance Inspector (QAI) in June 2018); however, the formal completion certificate is still pending, as some of the fencings of the motorway is yet to be completed coupled with finalizing pavement of side roads in some areas. M-9 offers various savings to commuters including lower vehicle operating cost, lesser time and distance which are not available in the alternative route. Toll collection from the road commenced in June 2018.

Business Update

Traffic Mix and Revenue

Actual traffic volumes during FY20 have been reported marginally higher than last year despite COVID-19 situation. In volumetric terms, major proportion of traffic accounts for cars, followed by multi axle and trucks.

	FY19	**FY20**
Revenue (Rs. In Mn)	5,691.2	5,536.9
Traffic Count (No. of Vehicles)	15,698,061	15,905,337
Proportion in Traffic Count		
	FY19	**FY20**
Cars	53.7%	57.3%
Wagons	5.2%	4.2%
Coasters	5.5%	5.8%
Buses	4.3%	3.2%
Trucks	12.6%	11.3%
Multi Axle	18.7%	18.2%
Total	**100%**	**100%**

Even though total traffic count displayed an uptick, overall revenue declined from Rs. 5.7bn to Rs.5.5bn. The core reason for this was the drop in traffic count of heavy vehicles (including Buses, Truck and Multi Axle) that pay higher toll fees. The reason for this drop in heavy vehicles was attributed to COVID-19 ensuing lockdown which slowed down the economic activities during the year. Hyderabad toll remained the highest revenue contributor with 45% of the share followed by Karachi and Kathore with 35% and 12%, respectively. Going forward, toll road revenue is forecasted to grow in FY21 & FY22 in tandem with positive economic growth projections. SCORE is focusing to generate other revenue sources besides toll roads. For this purpose, company is engaged in several business development activities, service stations and parking project. For FY20, income from other activities was meagre, contributing 0.4% of the top line for SCORE.

The company has encountered a few issues on account of adverse court rulings:

- The Sindh High Court (SHC) has ordered to stop collecting toll from Bahria Town Residents which consist of around 2-2.5% (estimated 0.3m/day) of the toll revenue of SCORE. The proceedings on this case in SHC is underway and the management of SCORE is confident of a positive outcome.

Profitability indicators have dropped in FY19-20, albeit are expected to rebound in FY21

- The company has commenced its operations in FY19 and posted a revenue of Rs. 5.7bn which lowered down to Rs. 5.5bn in FY20 amid COVID-19 situation.
- Gross margins declined to 28% in FY20 from 31% YoY due to lower revenue generation.

	FY19	FY20
Net Revenues	**5,691.2**	**5,536.9**
Gross Profit	**1,749.1**	**1,541.6**
Gross Margin	*30.7%*	*27.8%*
Administrative Expenses	60.6	56.2
Other Income	254.3	354.2
Operating Profit	**1,942.8**	**1,839.5**
Operating Margin	*34.1%*	*33.2%*
Finance Cost	2,726.6	3,338.5
Profit / (Loss) Before Tax	**(783.7)**	**(1,498.9**
Profit After Tax	**(705.0)**	**(1,582.0)**
Net Margin	**-12.4%**	**-28.6%**

- In FY21, profitability indicators are expected to improve, as economic activities started to pick pace from July 2020.
- As per management, actual toll collection for 9M'FY20 stood at Rs. 5.8b and the same is projected to grow to Rs. 7.5bn by year-end. In contrast, the expense base is also likely to be higher by ~Rs. 500mn, on account CCTV camera system installations and compliance with prime minister's green motorway initiative. Nevertheless, even after factoring in the same, net margin is expected to be more than 10% for FY21.
- Factoring in the 8% price escalation due by July 2021, revenue growth projections for FY22 are also on the higher side.

Key Rating Drivers

Unconditional guarantee from FWO

- The assigned rating factors in the unconditional guarantee of debt repayment provided by FWO in favor of SCORE.
- FWO is a military engineering organization established in 1966. Its objectives include projects related to civil, construction, combat, structural, and military engineering. The FWO led the design and construction of the Karakoram Highway. It builds civil and military infrastructure for the Government of Pakistan and the Pakistan Armed Forces.

Cash flow Coverage Indicators are expected to post improvement

- SCORE's debt profile primarily consist of long term loan and musharaka. The company's DSCR came under stress in FY20. This was mainly as a result of breach of covenants with lenders for Debt to Equity and Current Ration non-maintenance, as agreed. As a result, in FY19 accounts, the entire outstanding amount of debt was classified as current payable, thus adversely affecting the DSCR. The lenders, have subsequently given a waiver for SCORE and the accordingly, debt has been reclassified into current maturity and long term.

	FY19	FY20
Debt	23,407.0	20,938.0
FFO	2,444.2	1,556.0
FFO to Debt	10.4%	7.4%
DSCR	1.2x	0.29x

- Given revenue generated in 9MFY21, cash flow coverage of debt is expected to comfortably exceed 1.5x for FY21, while FFO to Debt is expected to rise above 20%.
- Further comfort is drawn from cash balance available, which amounted to Rs. 1.1bn as of Jun'20.
- Cash outflows in the rating horizon are limited albeit are expected to rise over the longer term, ahead of FY24-25 as the highway will require a layover after 7 years of operations.

Financial Risk:

- The company needs to increase its profits before taxation in order to generate ample cash for its debt servicing. If the cash generation remain stable in upcoming years, there could be a need for further cash injection in the company.

Business Risk:

- The core business of the company is to generate sustainable revenue over the rating horizon with gradual increase while the expected upcoming other revenue sources will provide strength to the topline.

Financial Summary (amounts in PKR millions)			Appendix I
	FY18	**FY19**	**FY20**
BALANCE SHEET			
Fixed Assets	32,510.6	29,391.0	26,478.6
Long term Advance	3,132.2	3,132.2	2,894.6
Stock-in-Trade	-	-	-
Trade Debts	-	-	-
Cash & Bank Balances	1,438.8	2,007.3	1,081.3
Total Assets	37,338.4	32,738.1	31,033.6
Trade and Other Payables	132.2	187.2	207.2
Long Term Debt (including current maturity)	24,997.0	23,407.0	20,938.0
Short Term Debt	-	-	-
Total Debt	24,997.0	23407.0	20,938.0
Total Liabilities	26,575.5	24,996.4	22,543.4
Paid-up Capital	10,800.0	10,800.0	10,800.0
Total Equity	10,762.9	10,058.3	8,490.2
INCOME STATEMENT			
Net Sales	0.0	5,691.2	5,536.9
Operating Profit	60.3	1,942.8	1,839.5
Profit Before Tax	47.2	-783.7	-1,498.9
Profit After Tax	34.3	-705.0	-1,568.1
RATIO ANALYSIS			
Net Profit Margin	N/A	-12.4%	-28.3%
Net Working Capital	(1,531.4)	(22,427.8)	-3,172.3
Current Ratio	0.5	0.1	0.3
ROAA (%)	0.1%	-1.9%	-4.7%
ROAE (%)	0.4%	-6.8%	-16.9%
Gearing (x)	2.3	2.3	2.5
Leverage (x)	2.5	2.5	2.7

ISSUE/ISSUER RATING SCALE &DEFINITIONS Appendix II

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	Superhighway Construction & Operation Rehabilitation Engineering (Private) Ltd.
Sector	Toll Roads
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-Mar-2021	AA-	A-1	Stable	Reaffirmed
30-Oct-2019	AA-	A-1	Stable	Reaffirmed
30-Nov-2018	AA-	A-1	Stable	Reaffirmed
21-Ocr-2016	AA-	A-1	Stable	Initial

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.
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