

## RATING REPORT

### Zephyr Power (Pvt.) Limited (ZPL)

**REPORT DATE:**

August 29, 2019

**RATING ANALYST:**

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**RATING DETAILS**

| Rating Category    | Latest Rating       |            | Previous Rating     |            |
|--------------------|---------------------|------------|---------------------|------------|
|                    | Long-term           | Short-term | Long-term           | Short-term |
| Entity             | A-                  | A-2        | A-                  | A-2        |
| <i>Rating Date</i> | <i>Aug 26, 2019</i> |            | <i>Aug 16, 2017</i> |            |
| Rating Outlook     | Stable              |            | Stable              |            |

**COMPANY INFORMATION**

|                         |  |
|-------------------------|--|
| Incorporated in 2005    | External Auditors: Deloitte Yousuf Adil      |
| Private Limited Company | Chief Executive Officer: Mr. Kumayl Khaleeli |

**APPLICABLE METHODOLOGY(IES)**

*Applicable Rating Criteria: Industrial Corporates (May, 2019)*. <https://s3-us-west-2.amazonaws.com/backupsqvis/docs/Corporate-Methodology-201904.pdf>

## Zephyr Power (Pvt.) Limited (ZPL)

### OVERVIEW OF THE INSTITUTION

Zephyr Power (Pvt.) Limited was incorporated as a private limited company in July 2005. The principal activity of the company is to build, own and operate wind power plant with a net capacity of 50MW in Gharo area, located in Thatta, Sindh.

### RATING RATIONALE

Incorporated in July 2005, Zephyr (Pvt.) Limited (ZPL) operates a 50.0MW (25 Wind Turbine Generators (WTGs) of 2.0MW generation capacity each) wind power plant in the Gharo area, Thatta, Sindh. Total cost of establishing the wind farm was USD 116.6m and the project was funded in a debt to equity ratio of 71:29. Commercial Operations Date (COD) was achieved on March 27, 2019. ZPL has claimed liquidated damages (LDs) from the EPC Contractor in line with the EPC agreement (10% of EPC cost) due to delay in CoD. Takeover by the management from the EPC contractor is expected to be completed by end-Sep 2019. ZPL has entered into an Energy Purchase Agreement (EPA) with Central Power Purchase Agency (Guarantee) Limited (CPPA-G) for a period of 20 years. Gamesa Wind (Tianjin) Co. Ltd is the O&M contractor for the first 10 years of the operations period.

#### Key Rating Drivers

##### Sound sponsor profile

The assigned ratings take into account sizeable equity stake of a Development Finance Institution (DFI) wholly owned by the UK Government. Ratings also incorporate experience of and sound profile of other three local equity shareholders.

##### Exposure to wind risk

The tariff of ZPL is approved under the Upfront Tariff Regime, 2015 from the National Electric Power Regulatory Authority (NEPRA); the tariff mandates that wind risk will be borne by the power producer. Hence, the power produced and cash flows are subject to seasonality in line with variation in the wind speed. However, the track record of generation so far coupled with the site specific Wind Resource Assessment studies conducted by three different consultants, use of efficient technology and presence of a fully funded Debt Service Reserve Account (DSRA), reduce the exposure to wind risk.

#### **Operational risk is considered manageable in view of the long term O&M contract in place with an experienced O&M operator**

As per the agreement, Gamesa Wind (Tianjin) Co. Ltd will act as the O&M operator for the first 10 years of the project since the Commercial Operations Date (CoD). O&M contractor has guaranteed to maintain 97% plant availability in the first year of operations and subsequently 98% for the remaining 9 years. The agreement mandates that the contractor will be liable to pay delay damages in case the plant availability is lower than the minimum guaranteed threshold. Moreover, the contractor has also provided warranty amounting to 10% of O&M contract price in this regard. Sound track record and extensive experience of Gamesa Wind (Tianjin) Co. Ltd provides comfort to managing operations risk.

**Presence of long term PPA with CPPA mitigates off-take risk while insurance coverage is also considered adequate**

In case of any capacity issue with the grid due to Non Project Events (NPEs), the company will continue to receive the revenues from CPPA under Non-Project Missed Volume (NPMV) which is compensation of loss of revenue. Furthermore, ZPL has adequate insurance cover for different events covered under the force majeure events.

**Satisfactory operating track record during first three months of the commercial operations**

With COD achieved in March 2019, the plant has operated successfully for the remainder of the ongoing year as per the management. During the first three months (April- June) of the operations, the month-wise average generation capacity has remained higher than 35% (stipulated in EPA) in high wind season and remained in line with projections. Maintaining the average capacity factor in line with the projections will continue to remain an important ratings consideration going forward.

**Figure 1: Production**

|                  | Apr  | May  | Jun  |
|------------------|------|------|------|
| Generation (GWh) | 14.9 | 21.3 | 19.4 |

**Sufficient cash flows (both current and projected) indicate satisfactory debt servicing ability; presence of a Debt Service Reserve Account (DSRA) provides comfort to the ratings. Erratic payment cycle exhibited by CPPA may translate into some liquidity pressures.**

Given the plant operated at a higher capacity than the required capacity, Funds from operations (FFO) during the first three months were adequate and are considered adequate to service outstanding debt obligations. Cash flows may witness seasonality on account of variation in wind speeds. Achievement of the projected financial milestones is critical from the ratings perspective. Going forward, as per the sensitized projected financials, projected cash flows are expected to remain sufficient to cover future debt repayments. Projected debt servicing coverage ratio (DSCR) also remains comfortable during the first ten years in which debt will be repaid. Furthermore, presence of Debt Service Reserve Account (DSRA) which covers 80% of the next principal payment and 300% of markup payment provides comfort to the ratings.

The energy sector's circular debt in the country was reported at Rs. 1.4 trillion at the beginning of 2019. Although the existing government is focused on reducing the quantum of circular debt, delays in payments by CPPA may translate into some liquidity pressures. However, the company has the option of using unutilized equity and contingency funds in such a situation. Excess equity amounting to USD 3.0 million is present that can be utilized to cover any shortfall.

**ISSUE/ISSUER RATING SCALE & DEFINITION**

**Annexure I**

**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](http://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](http://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](http://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               |                   |                       |                      |  |
|-------------------------------------|---|----------------------------|-------------------|-----------------------|----------------------|--|
| <b>Name of Rated Entity</b>         | Zephyr Power (Pvt.) Ltd.  |                            |                   |                       |                      |  |
| <b>Sector</b>                       | Power   |                            |                   |                       |                      |  |
| <b>Type of Relationship</b>         | Solicited   |                            |                   |                       |                      |  |
| <b>Purpose of Rating</b>            | Entity Rating   |                            |                   |                       |                      |  |
| <b>Rating History</b>               | <b>Rating Date</b>  | <b>Medium to Long Term</b> | <b>Short Term</b> | <b>Rating Outlook</b> | <b>Rating Action</b> |  |
|                                     | 26/08/2019  | A-                         | A-2               | Stable                | Reaffirmed           |  |
|                                     | 16/08/2017  | A-                         | A-2               | Stable                | Initial              |  |
| <b>Instrument Structure</b>         | N/A   |                            |                   |                       |                      |  |
| <b>Statement by the Rating Team</b> | 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.  |                            |                   |                       |                      |  |
| <b>Probability of Default</b>       | 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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