RATING REPORT

Shajar Roads Limited

REPORT DATE:
January 9, 2018

RATING ANALYSTS:

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RATING DETAILS

	Initial Rating	
Rating Category	**Long-term**	**Short-Term**
Entity	A	A-2
Rating Date	*January 4, 2018*	
Rating Outlook	Stable	

COMPANY INFORMATION

Incorporated in 2017	**Chief Executive Officer**: Mr. Mohsin Hussnain
Public Unlisted Company	
Key Shareholders (with stake 5% or more):	
Habib Construction Services - 51%	
Niaz Muhammad Khan & Brothers - 46%	

APPLICABLE METHODOLOGY(IES)

JCR-VIS Entity Rating Criteria: Industrial Corporates (May 2016)
http://jcrvis.com.pk/docs/Corporate-Methodology-201605.pdf
JCR-VIS Rating Criteria: Toll Roads Rating (December 2016)
http://jcrvis.com.pk/docs/MethToll201612.pdf

Shajar Roads Limited (SRL)

PROFILE

SRL has been incorporated as a public unlisted company in 2017. The shareholding of SRL is divided between three groups, namely Habib Construction Services (HCS) (51%), Niaz Muhammad Khan & Brothers (NKB) (46%) and Deokjae Construction Company Pakistan (DCCPL) (3%).

RATING RATIONALE

Shajar Roads Limited (SRL) has been established as a public unlisted company in order to undertake dualization and oversee management and maintenance of the existing 43km Sheikhupura – Gujranwala Road under the Build-Operate-Transfer (BOT) arrangement for the duration of the concession period. The company has entered into a concession with Government of Punjab (GoPb) for a period of 25 years. The project will be established under the Public Private Partnership (PPP) regime, with one of the sponsors, HCS, acting as the Engineering, Procurement & Construction (EPC) Contractor of the company. Management is targeting to achieve the financial close in Q1'18 and the projected construction time-period of the road is 1 year.

Rating Drivers:

Sponsor Profile: Ratings incorporate sound profile of the three sponsors of SRL. Shareholding of SRL is vested with Habib Construction Services (HCS), Niaz Muhammad Khan & Brothers (NKB) and Deokjae Construction Company Pakistan (DCCPL). Major stakeholders, HCS and NKB, have considerable experience in infrastructure projects and are considered to be financially sound. DCCPL has also been involved in construction and maintenance of Hyderabad-Mirpurkhas Dual Carriageway under BOT arrangement.

Demand Risk: As per the concession agreement, the demand risk is parked entirely with SRL and no minimum revenue guarantee has been provided by the GoPb. Thus, any shortfall in the projected revenues on account of decrease in projected volumetric traffic may have adverse impact SRL's debt repayment capacity. However, this risk is mitigated by factors such as conservative assumptions pertaining to traffic volumes incorporated in the financial model. Projected growth in volumes post dualization of the road has not been incorporated in the traffic volumes. Moreover, traffic volumes are in line with volumes specified in the traffic study conducted by the Communication and Works department of GoPb. Traffic profile features a diverse mix of commuter, agri and business related travel and is expected to remain moderately resilient to changes in economic cycles. Moreover, no competing or alternative route exists within a radius of 10 km of the route, if any such route is constructed, GoPb will compensate SRL for any loss in revenues. Since time savings over the course of the entire journey on this route would be significant, traffic volumes are expected to be sustainable. Growth in projected revenues is also a function of increase toll rates. The toll rates have been specified in the concession agreement and the same take into account the projected inflation. SRL will be compensated by the government in case toll rates are revised downwards.

Construction Risk: In case of delay in construction of the project, SRL is liable to pay construction damages to the government for the first 90 days of the delay beyond the substantial completion date. In case road completion is delayed by more than 90 days, GoPb reserves the rights to terminate the contract. Construction risk is minimal considering sound track record of EPC contractor, Habib Construction Services (HCS), which has completed several infrastructure projects in Punjab. Moreover, HCS intends to complete the project in a time span of 12 months, whereas the stipulated time period for the same is 21 months in the concession agreement. Hence, cushion for unanticipated delays exists. In case of delay of more than 21 months, the liability to pay liquidated damages to the government will be borne by HCS.

Costs Overrun Risk: Risk associated with changes in prices of raw materials shall be borne by SRL. As per management, changes in the prices of four major components including diesel, bitumen, steel and cement can have major impact on the overall costs of the project. In order to cover for such risk, management has already incorporated 5% contingency costs in the financial model. Moreover, procurement of majority of the material to be utilized in the construction of the road has already been undertaken. Hence, changes in prices of raw materials are expected to have minimal impact on the overall costs.

Financing Risk: Concession agreement mandates that SRL shall enter into a funding arrangement with the lenders and any subsequent changes in the financing costs would be incurred by SRL. In this regard, the company remains exposed to interest rate risk as the financing obtained is based on floating interest rate.

Debt Servicing: Liquidity profile of the company draws support from growing projected revenues and a structured mechanism in place, in the form of an escrow account, to facilitate timely repayments. Management will also maintain a Debt Service Reserve Account (DSRA) equal to two times of the next due debt payment at all times. Amount equal to one time of debt repayment is inbuilt in initial equity being injected in SRL, while the remaining amount will be accumulated through operations. Projected revenues are expected to remain sufficient to meet operating expenses and debt obligations of lenders. Leverage indicators are expected to improve gradually on the back of debt repayment and increase in total equity. Cushion in debt servicing is expected to remain at adequate levels even after sensitizing for lower revenues and higher costs.

ISSUE/ISSUER RATING SCALE & DEFINITIONS

Appendix I

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 II

Name of Rated Entity	Shajar Roads Limited
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				
4/1/2018	A	A-2	Stable	Initial

Instrument Structure	N/A
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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