RATING REPORT

Swat Expressway Planning Construction and Operations (Private) Limited (SEPCO)

REPORT DATE:
April 25, 2018

RATING ANALYSTS:
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RATING DETAILS

	Initial Rating	
Rating Category	**Long-term**	**Short-Term**
Entity	A-	A-2
Rating Date	*April 25, 2018*	
Rating Outlook	Stable	

COMPANY INFORMATION

Incorporated in 2016	**Chief Executive Officer**: Maj. Gen. Saeed Akhtar
Private Limited Company	**Chairman:** Lt Gen. Muhammad Afzal
Key Shareholders (with stake 5% or more):	**Independent Auditor:** Khalid Majid Rehman Chartered Accountants
Pakhtunkhwa Highways Authority	
Frontier Works Organization	

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

Swat Expressway Planning Construction and Operations (Private) Limited (SEPCO)

PROFILE

Swat Expressway Planning Construction and Operations (Private) Limited (SEPCO) was incorporated as a private limited company in 2016. Key sponsors include Pakhtunkhwa Highways Authority (PKHA) and Frontier Works Organization (FWO).

RATING RATIONALE

Incorporated in 2016, Swat Expressway Planning Construction and Operations (Private) Limited (SEPCO) is a Special Project Company (SPC) with registered office based in Rawalpindi. The company has entered into a concession agreement for a period of 25 years with Pakhtunkhwa Highways Authority (PKHA) for construction, management and maintenance of the Swat Expressway (SER); a project by Government of Khyber Pakhtunkhwa (GoKPK). The responsibility of road construction lies with Frontier Works Organization (FWO) while SEPCO will be responsible for operation and toll collection. SER will be constructed under the Build-Operate-Transfer (BOT) mode.

Rating Drivers

Sponsor Profile: Assigned ratings reflect sound profile of the two shareholders of SEPCO. Shareholding of SEPCO is vested with FWO (Class A shares) and PKHA (Class B shares). Major stakeholders, PKHA and FWO have considerable experience in infrastructure projects. FWO has undertaken major projects under public private partnership and BOT mandates. However, the ratings are constrained by absence of parent company guarantee and sponsor support agreement between SEPCO and the sponsor (FWO).

Revenue Risk (Volume): Traffic profile depicts that majority travel will pertain to tourism and commuter related travel. Since time savings over the course of the entire journey on this route would be significant (~2 hours) vis-à-vis competing route, traffic volumes are expected to be sustainable. Higher time taken over the competing route is a function of greater distance and challenging terrain of the road. If PKHA or any other public-sector entity decides to establish a competing route, then it will be ensured that the competing route shall be tolled at least equivalent to an amount 1.5 times higher than prevailing toll rates imposed at SER. Otherwise, SEPCO is entitled to receive losses in toll revenues from PKHA.

Revenue Risk (Price): Growth in projected revenues will also be a function of increase in toll rates, as specified in the concession agreement (CA). Toll rates will be revised upwards every year at a rate of 8%. Despite significant stake of GoKPK in the project, hindrance or political interference in increasing tolls is mitigated by contractual mechanism in place for increasing tolls. Apart from tolls, growth in revenues from other sources (service area) is expected; however, their proportion is expected to remain small. In case toll rates are revised downwards, SEPCO will be compensated by PKHA for loss in toll revenues.

Debt Servicing Coverage: Funding for project completion has almost entirely been arranged. Ratings are supported by existence of Operating Servicing Reserve Account (OSRA) with an amount equivalent to ~40% of the total debt; this has been built as part of the overall project cost. PKHA has injected its full equity and sub-ordinated loan amount. Rating also draws comfort from terms of the sub-ordinated loan where repayment is made in the last 5 years of the concession period. Liquidity profile draws support from projected growth in revenues. Debt repayment capacity of SEPCO may be affected in case traffic volumes are lower than projected. Gross revenue is expected to increase on account of growth in traffic and escalation in toll rates. With higher profitability, FFO is expected to increase steadily over the years. Debt servicing is low in the initial years but is projected to increase with growth in traffic and increase in toll rates. The company will have to utilize built in reserves for meeting shortfall in debt repayment.

Project Completion/Maintenance: Regular maintenance of the road is outsourced to FWO while documented maintenance manual is in place. Major overhaul of the road is due in 2027 and 2038. As per agreement, the completion date of the project is envisaged for May'2019. Given the current pace of work, management expects significant completion by last quarter of 2018. This is expected to result in a cash flow accumulation of one year before debt repayment commences on 30 November'2019.

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	Swat Expressway Planning Construction and Operations (Private) Limited (SEPCO)
Sector	Toll Roads
Type of Relationship	Solicited
Purpose of Rating	Entity rating
Rating History	see table below
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.
Probability of Default	JCR-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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Rating History

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
RATING TYPE: ENTITY				
25-Apr-18	A-	A-2	Stable	Initial