RATING REPORT

Artistic Energy (Pvt.) Limited

REPORT DATE:
April 9, 2019

RATING ANALYSTS:

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RATING DETAILS				
	Latest Rating		**Previous Rating**	
Rating Category	**Long-term**	**Short-term**	**Long-term**	**Short-term**
Entity	A	A-1	A	A-1
Rating Date	*April 9, 2019*		*June 26, 2018*	
Rating Outlook	Stable		Stable	
Rating Action	Reaffirmed		Initial	

COMPANY INFORMATION	
Incorporated in 2014	**External auditors:** M/s EY Ford Rhodes Sidat Hyder
Private Limited Company	**Chairman of the Board:** Mr. Yaqoob Ahmed
Key Shareholders (with stake 5% or more):	**Chief Executive Officer:** Mr. Yaqoob Ahmed
Artistic Milliners (Pvt.) Limited (AML) – 99.9%	

APPLICABLE METHODOLOGY(IES)
Applicable Rating Criteria: Industrial Corporates (May, 2016) ***http://www.vis.com.pk/kc-meth.aspx***

Artistic Energy (Pvt.) Limited (AEL)

OVERVIEW OF THE INSTITUTION

Artistic Energy (Pvt.) Limited (AEL) was incorporated as a private limited company in 2014. AEL is principally engaged to maintain wind power generation project of 49.3MW for the generation and supply of electric power. Registered office of the company is located in Karachi.

Financial Statements of the company for FY18 were audited by M/s EY Ford Rhodes Sidat Hyder. Auditors belong to category 'A' on the approved list of auditors published by the State Bank of Pakistan (SBP).

Profile of CEO & Chairman

Mr. Yaqoob Ahmed is the Chairman and Chief Executive of the Company of AEL. He is also the Chairman and CEO of Artistic Milliners (Pvt.) Ltd. He has over 40 years of experience in the textile sector.

Financial Snapshot

Net Equity: *Dec'18: Rs. 4.0b, June'18: Rs. 3.5b*

Net Revenue: *HFY19: Rs. 1.5b, FY18: Rs. 1.3b*

RATING RATIONALE

Incorporated in 2014, Artistic Energy (Pvt.) Limited (AEL) operates a 49.3MW (29 Wind Turbine Generators (WTGs) of 1.7 MW generation capacity each) wind power plant in Jhimpir, District Thatta, Sindh which was set up at a total cost of Rs 11.7b. The project was funded in a debt equity ratio of 75:25. The plant started commercial operations in March'2018. The company has signed a twenty year Energy Purchase Agreement (EPA) with Central Power Purchasing Agency (CPPA) at a levelized tariff rate of Rs 12.71 per kWh. The Engineering, Procurement and Construction (EPC) were jointly undertaken by Hydrochina International Engineering Co., Ltd. (HIEC) and Hydrochina Corporation while HIEC is responsible for operations & maintenance (O&M) during the initial 2 years of operations till June'2020.

Key Rating Drivers

Strong sponsor profile

Assigned ratings continue to draw comfort from strong sponsor profile. The company is a wholly owned subsidiary of Artistic Milliners (Pvt.) Limited (AML). AML has been assigned a credit rating of AA-/A-1 from VIS Credit Rating indicating high credit quality and strong protection factors.

Exposure to wind risk.

Power produced and in turn cash flows are susceptible to seasonality and possible variance in wind speed. Nonetheless, the track record of generation so far in addition to a site specific Wind Resource Assessment and Energy Yield Evaluation Study conducted by Lahmeyer International Germany confirming the adequate wind availability historically provides comfort against this risk.

Operational risk is considered manageable given long-term O&M contract in place with experienced O&M operator.

As per initially agreed terms, 2-year O&M contract with HIEC will end in June'2020. Subsequently, General Electric (GE) will manage the operations and maintenance for next eight years with provisions for ensuring minimum 97% availability of WTGs. In case of availability remaining lower than the agreed level, GE is liable to pay liquidated damages. Moreover, sound track record and extensive experience of both O&M operators, HIEC and GE, in renewable energy sector provides comfort to managing operations risk.

Presence of long term Energy Purchase Agreement with CPPA mitigates off-take risk while adequate insurance coverage is in place.

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, AEL has adequate insurance cover for different events covered under the force majeure events.

Satisfactory operating track record during 1st year of commercial operations.

The wind farm has completed 12 months of successful operations with average generation capacity and plant availability remaining compliant with normative parameters as laid down in the EPA. During the period under review, month-wise average generation capacity has remained significantly higher than 35% (stipulated in EPA) in high wind season (April-September) of FY18. However, plant availability was impacted for select months due to a technical fault in one WTG. Besides the aforementioned reason, generation was also lower during October'2018 and November'2018 due to seasonal variation in wind speed. Capacity factor and plant availability for the period March'2018 to Dec'2018 is presented in the table below:

Table 1: Performance Indicators (Month-wise)

	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
Generation MW	8,216	19,251	23,348	27,089	28,760	25,617	21,219	7,586	8,518	10,452
Generation %	22.2%	53.8%	63.1%	75.6%	77.7%	69.2%	59.3%	20.5%	23.8%	28.25%
Availability %	98.2%	98.1%	95.6%	98.5%	99.2%	97.3%	90.3%	81.1%	92.1%	96.8%

Sound debt coverage metrics (present and projected) and sufficient cash flows indicate satisfactory debt servicing ability; however, erratic payment cycle exhibited by CPPA may translate into some liquidity pressures.

During FY18, Funds from operations (FFO) amounted to Rs. 1.15b (for 4 months of operations) while FFO during HFY19 amounted to Rs. 1.2b. Debt Servicing Coverage ratio and FFO to Total Debt remain sound at 1.75x and 0.22x during HFY19, respectively. Going forward, as per the sensitized projected financials, cash flows are expected to remain sufficient for future debt repayments. Projected debt servicing coverage ratio (DSCR) also remains comfortable during the first ten years in which debt will be repaid.

The energy sector's growing circular debt in the country had reached Rs. 1,362 billion mark as at end-2018. Given the rising circular debt, delays in payments by CPPA may translate into some liquidity pressures. However, in case AEL acquires short term financing facility for liquidity management, CPPA will compensate through a fixed mark-up payment. Total overdue receivables of AEL decreased to Rs. 791.1m (FY18: Rs. 1.42b) at end-HFY19. Going forward, receipts from recent issuance of Rs. 200b circular debt Sukuk by the government along with another issuance planned will facilitate in managing outstanding receivables. The Company has a running finance line of Rs. 750m in place to fund any shortfalls.

High leverage indicators due to sizeable dividend payout and debt levels

Total equity of AEL has increased to Rs. 4.0b (FY18: Rs. 3.5b) at end-HFY19. Total unappropriated profit amounted to Rs. 1.1b (FY18: Rs. 552.0m) at end-HFY19 which has been paid out as dividends in January'2019. Management expects payout levels to remain elevated over the rating horizon. Total debt carried on balance sheet (including supplier credit) is long term in nature amounting to Rs. 10.8b (FY18: Rs. 11.0b) at end-HFY19. Long-term debt profile includes loans from commercial banks along with a supplier's credit, amounting Rs. 2.4b (USD 16m), mobilized for purchase of plant and machinery. In order to pay off this foreign currency debt, the company has acquired a local currency loan of Rs. 2.2b, proceeds of which have been placed in the form of TDRs. As per management, returns from these deposits are expected to hedge against the foreign liability's prevailing currency risk. However, in case rupee depreciation is in excess of return on TDR, the company will incur an exchange loss. Gearing and leverage ratios were reported at 2.70x (FY18: 3.17x) and 2.79x (FY18: 3.25x) respectively at end-HFY19. Going forward, level of leverage indicators will depend on quantum of dividend payout and borrowings mobilized, if any, to fund working capital requirements.

Artistic Energy (Pvt.) Limited (AEL) Annexure I

FINANCIAL SUMMARY		*(amounts in PKR millions)*
BALANCE SHEET	**FY18 (4 Operating Months)**	**HFY19**
Property, Plant and Equipment	10,751.8	10,480.7
Debtors	1,061.6	791.1
Short Term Investments	-	3,151.5
Cash & Bank Balances	2,726.1	588.3
Total Assets	14,753.0	15,184.7
Trade and Other Payables	140.4	194.3
Long Term Debt	11,023.5	10,791.5
Total Equity	3,474.2	4,004.1
INCOME STATEMENT		
Net Sales	1,267.8	1,543.1
Gross Profit	930.7	1,028.3
Operating Profit/Loss	918.8	1,012.7
Profit After Tax	567.7	529.9
RATIO ANALYSIS		
Gross Margin (%)	73.4%	66.6%
Net Working Capital	2,635.7	3,119.9
FFO to Total Debt (%)	0.10	0.22
FFO to Long Term Debt (%)	0.10	0.22
Debt Servicing Coverage Ratio (x)	7.36	1.75
ROAA (%)	6.1%	7.1%
ROAE (%)	25.7%	28.3%
Gearing (x)	3.17	2.70
Leverage (x)	3.25	2.79

ISSUE/ISSUER RATING SCALE & DEFINITION 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	Artistic Energy (Pvt.) Ltd.
Sector	Power
Type of Relationship	Solicited
Purpose of Rating	Entity Rating
Rating History	

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
4/9/2019	A	A-1	Stable	Reaffirmed
6/26/2018	A	A-1	Stable	Initial

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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