RATING REPORT

Artistic Energy (Pvt.) Limited

REPORT DATE:
March 16, 2021

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	*March 16, 2021*		*March 16, 2020*	
Rating Outlook	Stable		Stable	
Rating Action	*Upgrade*		Reaffirmed	

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. Muhammad Murtaza Ahmed
Artistic Milliners (Pvt.) Limited (AMPL) – 99.9%	

APPLICABLE METHODOLOGY(IES)

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

Artistic Energy (Pvt.) Limited (AEPL)

OVERVIEW OF THE INSTITUTION

Artistic Energy (Pvt.) Limited (AEPL) was incorporated as a private limited company in 2014. AEPL 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 FY20 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 Chairman

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

RATING RATIONALE

Incorporated in 2014, Artistic Energy (Pvt.) Limited (AEPL) 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). The Engineering, Procurement and Construction (EPC) were jointly undertaken by Hydrochina International Engineering Co., Ltd. (HIEC) and Hydrochina Corporation while HIEC was responsible for operations & maintenance (O&M) during the initial 2 years of operations till June 2020. Subsequently, General Electric (GE) will manage the operations and maintenance for next eight years.

Master Agreement signed with CPPA

Under the committee for negotiations with IPPs and GoP, AEL has signed a master agreement on February 12, 2021 encompassing alterations in in the existing contractual arrangements. The purpose of the same is to improve liquidity profile of the company through swift clearing of outstanding dues by the GoP. The GoP has already submitted the Tariff Adjustment Application to NEPRA. Consequently, revised tariff shall be applicable when the last payment has been made by the GoP to AEL. However, on agreement of both the parties, AEL shall commence giving discounts in the tariff once the first installment is paid. The following are the key terms of the agreement:

1. ROE shall be reduced to 13% per annum
2. The debt tenor shall be increased by 5 years and the existing spread shall be reduced by 125bps over the KIBOR
3. Existing O&M annual component shall be reduced by 20%
4. Cap for the amount of insurance during operation shall be reduced to 0.7% of the EPC cost.

As a result of the aforementioned clauses, management expects its tariff to reduce by around Rs. 1.89/Kwh. Latest quarterly indexed tariff was Rs. 16.53/Kwh. Under the agreement, payment mechanism of outstanding receivables at end-Nov'20 to the tune of Rs. 2.3b entails payment to be made in 2 installments with 40% being paid in the first installment and the remaining 60% to be paid within six months from the date of the first disbursement. Installments shall be received in the following mode:

- 1/3rd in cash,
- 1/3rd in the form of tradable 10 year floating rate PIBs, and
- 1/3rd in the form of tradable 5 year floating rate GoP Ijarah Sukuks.

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 (AMPL). AMPL has been assigned a credit rating of AA-/A-1 by VIS Credit Rating Company indicating high credit quality, strong protection factors and high likelihood of support if required.

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 ended in June 2020. Subsequently, General Electric (GE) shall be managing 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, AEPL has adequate insurance cover for different events covered under the force majeure events.

Satisfactory operating track record since commercial operations.

The wind farm has completed around three years of successful operations with average annual generation capacity and plant availability remaining compliant with normative parameters as laid down in the EPA. During FY20, average capacity factor was reported at 40.1% being higher than 35% as stipulated in EPA. While remaining above the 35% stipulated in the EPA, the same witnessed some decline during the ongoing year owing to lower wind speed during summer season. Plant availability remained above 97% during the review period. Monthly energy delivered and plant utilization factor for 2020 is demonstrated in the following table:

2020	Jan	Feb	Mar	April	May	Jun	July	Aug	Sep	Oct	Nov	Dec
Net Energy Delivered (MW)	9,856	10,963	10,045	14,594	22.743	21,281	18,250	18,053	12,948	9,733	10,649	14,474
Plant Utilization Factor (%)	26.87%	33.09%	54.74%	41.11%	62.01%	59.95%	49.76%	49.22%	36.48%	26.54%	30.00%	39.46%

	FY18	FY19	FY20	1HFY21
Capacity factor (Actual)	61.16%	47.38%	40.06%	38.58%
Availability	97.52%	97%	98.49%	99.05%

Sound debt coverage metrics (present and projected) and sufficient cash flows indicate satisfactory debt servicing ability. Moreover, recent MOU signed with the GoP may further improve liquidity profile once a sizeable chunk of the outstanding trade debts are received

During FY20, Funds from operations (FFO) improved to Rs. 2b (FY19: Rs. 1.65b; FY18: Rs. 796.5m). Debt Servicing Coverage ratio and FFO to Total Debt remain sound at 1.37x and 25.4% during FY20, respectively. Despite expected decline in tariff, projected debt servicing coverage ratio (DSCR) is expected to remain comfortable over the rating horizon. The company did not pay dividends in the outgoing year.

The energy sector's growing circular debt in the country had reached Rs. 2.03 trillion mark as at end-Nov'20. In order to reduce the same, the GoP has been undergoing negotiations with the IPPs. In pursuant to the master agreement discussed above, liquidity profile of the company is expected to improve going forward, once the GoP clears AEL's outstanding dues in two tranches.

Improving leverage indicators due to increase in equity base owing to profit retention

Equity base of AEPL has increased to Rs. 5.7b (FY20: Rs. 4.9b; FY19: Rs. 3.5b) at end-HFY21 due to profit retention and no dividend payout during FY20 and 1HFY21. Total adjusted debt carried on balance sheet (including supplier credit and adjusting for short term investments) amounted to Rs. 7.5b (FY20: Rs. 7.9b) at end-December 2020. Long-term debt profile includes loans from commercial banks along with a supplier's credit, amounting Rs. 2.0b 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. Gearing adjusted for short term investments improved on account of higher equity base and was reported at 1.31x (FY20: 1.60x, FY19: 2.63x) at end-1HFY21. 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 (AEPL) Annexure I

FINANCIAL SUMMARY *(amounts in PKR millions)*					
BALANCE SHEET	**FY17**	**FY18**	**FY19**	**FY20**	**1HFY21**
Paid Up Capital	154	2,922	2,922	2,922	2,922
Total Equity	946	3,692	3,550	4,974	5,716
INCOME STATEMENT					
Net Sales	-	1,161	3,101	2,973	1,421
Profit Before Tax	(5)	793	1,721	1,432	755
Profit After Tax	(5)	786	1,696	1,424	752
RATIO ANALYSIS					
FFO	(4)	797	1,651	2,013	795
Current Ratio (x)	7.53	3.10	1.80	2.30	4.06
Gearing (x)-adjusted	2.88	2.99	2.63	1.60	1.31

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**	
	3/16/2021	A+	A-1	Stable	Upgrade	
	3/16/2020	A	A-1	Stable	Reaffirmed	
	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.					
Disclaimer	Information herein was obtained from sources believed to be accurate and reliable; however, VIS does not guarantee the accuracy, adequacy or completeness of any information and is not responsible for any errors or omissions or for the results obtained from the use of such information. For conducting this assignment, analyst did not deem necessary to contact external auditors or creditors given the unqualified nature of audited accounts and diversified creditor profile. 					
Due Diligence Meetings Conducted		**Name**	**Designation**	**Date**		
	1	Mr. Rafique Khanani	CFO and Company Secretary	26-Feb-2021		
	2	Mr. Irfan Bashir	General Manager	26-Feb-2021		
	3	Mr. Ali Iqbal	Finance Manager	26-Feb-2021		