RATING REPORT

Gharo Solar Limited

REPORT DATE:
September 12, 2023

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	September 12, 2023		September 6, 2022	
Rating Outlook	Stable		Stable	
Rating Action	Reaffirmed		Reaffirmed	

COMPANY INFORMATION	
Incorporated in 2016	**External auditors:** KPMG Taseer Hadi & Co. Chartered Accountants
Public Unlisted Company	**Chairman:** Rana Nasim Ahmed **CEO:** Rana Uzair Nasim
Key Shareholders (with stake 5% or more):	
Rana Nasim Ahmed – 55%	
Windforce (Private) Ltd – 30%	
Norsk Solar – 10%	
Mohammad Khaqan Babar Cheema – 5%	

APPLICABLE METHODOLOGY(IES)
Applicable Rating Criteria: **Corporates (May 2023)** https://docs.vis.com.pk/docs/CorporateMethodology.pdf **Rating Scale & Definitions** https://docs.vis.com.pk/docs/VISRatingScales.pdf

OVERVIEW OF THE INSTITUTION

Gharo Solar Limited was incorporated in June, 2016, as a private limited Company under the repealed Companies Ordinance, 1984 (now Companies Act, 2017). Subsequently, the Company changed its legal status from private to public limited company on January 01, 2019. The Company owns and operates a solar power plant of 50 MW generation capacity.

Profile of CEO: Rana Uzair Nasim is also the CEO of Harappa Solar (Pvt) Ltd and has led the project from inception through commissioning and operations. He has previously worked as a management consultant in New York with Oliver Wyman and Dalberg Global Development Advisors. He holds a BA degree in Economics and and MS degree in Management Sciences & Engineering, both from Stanford University, California, USA.

RATING RATIONALE

Incorporated in 2016, Gharo Solar Limited ('GSL' or 'the company') is a public unlisted company engaged in the generation and supply of electricity to K-Electric through a 50 MW solar PV power plant near Gharo, District Thatta, Sindh. The plant was constructed at a total cost of ~ Rs. 6.3b with debt-to-equity ratio of 75:25. The ratings draw comfort from the EPA (Energy Purchase Agreement) being signed with K-Electric on 'take or pay' provision, valid for 25 years from the commercial operation date (COD). The plant must run under no merit listings due to solar power being a renewable resource. The ROE (return on equity) component of the tariff for the project was determined at 15%. The company has opted for cost-plus tariff structure.

The project sponsors include local sponsors with extensive experience in solar power sector and international players having considerable expertise operating renewable energy projects around the world. The solar power plant started commercial operations in December 2019. According to the management, GSL has not faced any curtailments since commercial operations started more than three and half years ago.

Key Rating Drivers

Sound sponsor profile: The ratings incorporate sound profile of local and international sponsors having considerable experience in setting up green-field projects in power and industrial sectors. Chairman, Mr. Rana Ahmed holds major stake at ~55% is also the main sponsor of Harappa Solar, an 18MW solar PV power plant under operation near Sahiwal. Other significant shareholder, Windforce (Pvt.) Ltd (~30%) is a leading private sector power producer in Sri Lanka with diversification into wind, solar, and hydro power across various countries in the world. Apart from Pakistan, Windforce has plants established in Uganda and Ukraine as well and is conducting feasibility studies to expand further across the globe. Norsk Solar that holds ~10% stake, is a Norwegian based vertically integrated IPP (Independent Power Producer) and focuses on building solar projects in emerging markets. Leveraging experience in solar power, the primary sponsors have entered bids in some other renewable power projects in the country as well.

Sound operating performance observed on a timeline basis: The annual benchmark electricity generation for GSL based on 22.21% capacity factor is 97,279.8 MWh. However, the plant has been performing well above the NEPRA laid performance parameters and produced a higher output than the benchmark level in each year of operation with a capacity factor hovering above an average of 23-24% since commencing operations. The plant's capacity factor reached 23.31% (FY22: 23.72%) in FY23. Under the EPA, GSL will further reap the benefit from producing electricity beyond the benchmark capacity factor in the form of higher tariff payments. Annual degradation factor of 0.5% is considered for each operating year whereas plant availability remains above 99% during peak summer months.

	FY21	FY22	FY23
Installed capacity-Kilowatts	50,000	50,000	50,000
Annual benchmark energy-kWh	97,279,800	97,279,800	97,279,800
Actual energy delivered-kWh	108,626,026	102,644,000	102,092,092

To effectively utilize solar energy, the company has installed PV solar plant for the first time in Pakistan. It has a bi-facial solar technology and single axis trackers, along with sun tracking technology, which helps in absorbing the maximum amount of solar radiation to convert it into power. Also, the company has installed dual glass technology to avoid abrasion and cope up with the variance in temperature levels. The company's total fixed assets increased to Rs. 7.7b (end-FY22: Rs. 6.4b) by end-FY23 on the account adjustments relative to capitalized foreign exchange loss amounting Rs. 1.5b (FY22: Rs. 922.5m) to plant and machinery.

Presence of long-term Energy Purchase Agreement with K-Electric and O&M contract with experienced operator, mitigates operational risk: The electricity generated is purchased by K-Electric under the EPA dated September 26, 2018 which is valid for 25 years from the COD. In case K-Electric is unable to accept all energy delivered, this will constitute as Non-Project Event (NPE) and GSL will continue to receive the payments from K-Electric under Non-Project Missed Volume (NPMV), in compensation of revenue loss. Furthermore, even if the plant remains non-operational for a period due to any reason, K-Electric is liable to pay GSL for those days on the basis of expected units determined by an independent valuator. Probability of the same is on the lower side since the plant is classified as a must-run plant in the merit order.

Revenue from K-Electric is invoiced monthly and the payment mechanism is executed through an escrow account where K-Electric is required to pay within 30 days once the invoice is received. The escrow mechanism allows direct transfer to GSL's revenue account before K-Electric can access its account for other transactions. In case of delayed payment, the K-Electric is liable to pay markup at the rate of KIBOR plus 2% on prorated basis for the delayed period. To-date all payments have been received on time.

As per initially agreed terms, the company signed a three year long O&M (Operations and Maintenance) contract with OMS (Pvt.) Ltd in 2018 that ended in Dec'22 after the completion of first term. The O&M has been renewed for three more years on similar terms. OMS (Pvt.) Ltd has a sound track record and extensive experience in renewable energy sector with notable clients including Orient Power Company Limited, Packages Limited, JDW Power (Private) Ltd., K-Electric, Punjab Thermal Power Limited, and Northern Power Generation Company Limited. This, coupled with the fact that the OMS (Pvt.) Ltd. has been the O&M operator of the other power plant of the group as well, provides comfort against operational risk.

Growing profitability: Topline of the company reached Rs. 1.5b (FY22: Rs. 1.0b, FY21: Rs. 1.3b) in FY23 on the account of increase in tariff which is indexed on a quarterly basis. The company's energy supplied to K-Electric remained around similar levels (FY23: 102,092,092 MWh, FY22: 102,644,000 MWh). Delay in true-up tariff determination by NEPRA, resulted in tariff adjustment for two years in FY21 led to higher sales for that year and therefore reflects in lower sales for FY22. Quarterly tariff indexation is applicable since Jul'21, with the latest rate being approved at Rs. 17.8/kWh (for Jul-Sep'23) against a levelized tariff awarded at Rs. 8.7/kWh (Apr'21).

Given the company's inherent business model, margins have remained sound. Direct costs increased to Rs. 441.3m (FY22: Rs. 367.1m) and administrative expenses at Rs. 95.1m (FY22: Rs. 63.5m) in FY23. GSL made healthy return on its short-term investments adding to additional income of Rs. 129.8m (FY22: Rs. 78.4m) in FY23. As a result, operating profit stood higher at Rs. 921.8m (FY22: Rs. 565.8m) in FY23. Financial cost increased by 75.3% in FY23 on account of hike in policy rate and higher average borrowings on the balance sheet. Taxation is only charged on income made from investments in financial assets; taxation stood at Rs. 19.2m (FY22: Rs. 14.7m) in FY23. GSL's bottom-line increased to Rs. 489.3m in FY23 that was 55.6% higher than FY22.

Sound liquidity profile: In line with growing profits, funds from operations (FFO) increased to Rs. 777.4m (FY22: Rs. 581..0m) in FY23. Coverages have remained range bound. Current ratio has remained adequate. Comfort is drawn from the presence of Debt Service Reserve Account for debt repayments wherein GSL has invested Rs. 493.2m (Jun'22: Rs. 541.1m) of excess cash accumulation in mutual funds against the minimum requirement of Rs. 300m as of Jun'23. Consequently, portfolio of short-term investments also provides support to the liquidity profile of the company. Outstanding dues from K-Electric past 90 days reached Rs. 180.2m (FY22: Rs. 153.4m, FY21: Rs. 130.6m) in FY23. However, liquidity risk is mitigated by sound liquidity indicators, further augmented by healthy Debt Service Reserve Account.

Equity base improved in FY23 due to profit retention: Equity base of GSL improved to Rs. 2.3b (FY22: Rs. 1.9b, FY21: Rs. 2.3b), given that in FY22 dividend payout of Rs. 650.2 million was above net profit in the same year as opposed to profit retention in FY23 exceeding dividend payout of Rs. 140.3 million. Due to a depreciation of local currency against USD, quantum of foreign debt in rupee terms increased. As per accounting standards, the company is not allowed to adjust dollar-based equity in the same manner as debt.

Gearing and leverage ratios were therefore reported range bound at 2.82x (FY22: 2.80x, FY21: 2.16x) and 2.89x (FY22: 2.87x, FY21: 2.18x) respectively, at end-FY23. Despite profit retention and resultant increase in equity base, gearing may remain around current levels due to the impact of currency devaluation on foreign borrowings.

Gharo Solar Limited Annexure I

FINANCIAL SUMMARY	*(amounts in PKR millions)*		
BALANCE SHEET	**FY21**	**FY22**	**FY23**
PP&E	5,762.3	6,445.1	7,685.4
Trade Debts	237.4	278.9	409.4
Short Term Investments	420.8	541.1	493.2
Cash & Bank Balance	240.8	142.8	184.1
Other Assets	608.9	140.0	171.4
Total Assets	**7,270.3**	**7,547.9**	**8,943.4**
Trade & Other Payables	45.4	136.1	163.1
Long-Term Borrowings *(inc. current maturity)*	4,936.7	5,459.2	6,478.5
Other Liabilities	3.6	4.6	4.8
Total Liabilities	**4,985.6**	**5,599.9**	**6,646.3**
Paid Up Capital	1,002.1	1,002.1	1,295.4
Total Equity	**2,284.6**	**1,948.0**	**2,297.0**
INCOME STATEMENT	**FY21**	**FY22**	**FY23**
Net Sales	1,259.6	996.4	1,458.2
Gross Profit	898.7	629.3	1,016.9
Finance Cost	306.7	315.1	543.1
Profit Before Tax	565.1	329.1	508.6
Profit After Tax	**558.8**	**314.4**	**489.3**
RATIO ANALYSIS	**FY21**	**FY22**	**FY23**
Gross Margin (%)	71.3%	63.2%	69.7%
Net Margin (%)	44.4%	31.6%	33.6%
FFO	815.7	581.0	777.4
FFO to Total Debt (x)	16.5%	10.6%	12.0%
Debt Servicing Coverage Ratio (x)	1.61	1.28	1.31
Current Ratio (x)	3.42	1.81	1.67
ROAA (%)	7.6%	4.2%	5.9%
ROAE (%)	27.9%	14.9%	23.1%
Gearing (x)	2.16	2.80	2.82
Debt Leverage (x)	2.18	2.87	2.89

REGULATORY DISCLOSURES — Annexure II

Name of Rated Entity	Gharo Solar Limited
Sector	Power
Type of Relationship	Solicited
Purpose of Rating	Entity Ratings

Rating History

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
RATING TYPE: ENTITY				
12/09/2023	A	A-1	Stable	Reaffirmed
06/09/2022	A	A-1	Stable	Reaffirmed
27/10/2021	A	A-1	Stable	Upgrade
11/08/2020	A-	A-2	Stable	Reaffirmed
03/05/2019	A-	A-2	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.
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Due Diligence Meetings Conducted

Name	Designation	Date
Mr. Husnain Arif	Chief Financial Officer	August 15, 2023
Mr. Kamil Munir	Assistant Manager Accounts and Finance	August 15, 2023
Mr. Muhammad Sahal	Assistant Manager Treasury	August 15, 2023