RATING REPORT

Mega Conglomerate (Private) Limited

REPORT DATE:
August 1, 2018

RATING ANALYSTS:
Talha Iqbal
talha.iqbal@jcrvis.com.pk

Muhammad Ibad Desmukh
ibad.deshmukh@jcrvis.com.pk

RATING DETAILS		
	Initial Rating	
Rating Category	**Long-term**	**Short-term**
Entity	AA-	A-1
Rating Outlook	Stable	
Rating Date	*July 10, 2018*	

COMPANY INFORMATION	
Incorporated in 2010	**External auditors:** Muniff Ziauddin & Co. Chartered Accountants
Private Limited Company	**Chairman of the Board:** Mr. Habibullah Khan
Key Shareholders (with stake 5% or more):	**Chief Executive Officer:** Mr. Habibullah Khan
Mega & Forbes Group of Companies – 100%	

APPLICABLE METHODOLOGY(IES)
Applicable Rating Criteria: Industrial Corporates (May, 2016)
http://jcrvis.com.pk/docs/Corporate-Methodology-201605.pdf

Mega Conglomerate (Private) Limited

OVERVIEW OF THE INSTITUTION

Mega Conglomerate (Private) Limited was incorporated as a private limited company in 2010 under Companies Ordinance, 1984. Registered office of the company is in Karachi, Pakistan.

Profile of Chairman and CEO
Mr. Habibullah Khan is the founder of Mega & Forbes Group of Companies. He is a very well-known businessman and industrialist.

RATING RATIONALE

Mega Conglomerate (Private) Limited (MCPL) operates under a holding company structure. The company was setup as a wholly owned investment arm of Mega & Forbes Group of Companies (MFG), envisioned to realize synergies across the group's portfolio through innovative expansion with an aim to achieve consistent steady growth. Largest investment on balance sheet is in The Hub Power Company Limited (Hubco) shares representing around 80% of total assets. The company has two other investments, 100% stakes in VMFG (Private) Limited (VMFG) and G4 Mega Pakistan (Private) Limited (G4), through which it has exposure in the consumer goods (Haleeb Foods Limited - HFL) and real estate development (Imperial Developers and Builders Private Limited - IDBL) sectors.

Strong sponsor profile with diversified operations and revenue streams
While initially present in the shipping sector, MCPL's sponsor, MFG, has since established presence across a diversified range of sectors – namely telecommunications, logistics, construction materials, and through MCPL, in the energy, real estate development and consumer goods industries. MFG's business position stems from its prominent position in the shipping sector, representing 13 shipping lines (including 6 of the top 20 global container carriers in Pakistan) with a combined market share of over 19% of total containerized throughput of the country; this segment has been generating healthy cash flows over the years. MFG also operates a unit involved in downstream container operations of MFG as well as another company, which is the authorized distributor of Motorola's two-way radios for over four decades. MFG acquired International Organization for Standardization 9001:2000 (Quality Management System) certification in 1999; the same has been upgraded to 9001:2008.

Stable projected dividend income from investments
Balance sheet footing of MCPL stood at Rs. 29.4b (FY17: Rs. 1.2b) at end-9MFY18. The company has Rs. 2.4b parked in saving accounts and Rs. 2.3b in Term Deposit Receipts (TDRs) as at March 31, 2018. In line with its mandate, MCPL has 19.39% interest in Hubco amounting to Rs. 23.6b and 100% stake in subsidiaries – VMFG and G4, amounting to Rs. 898.5m and Rs. 280.5m respectively.

<u>Hub Power Company Limited</u>
Hubco is the largest independent power producer (IPP) in the country. Under its belt is a 1,200MW Furnace Oil (RFO) based power station situated in Baluchistan (Hub Plant; commissioned in 1997), a wholly owned 214MW RFO fired power station in Punjab (Narowal Plant; commissioned in 2011) in addition to 75% controlling interest in 84MW hydel power project (Laraib Energy Limited; commissioned in 2013). In line with business strategy, Hubco is now in process of constructing a 1,320MW coal fired power plant (2x660MW) in collaboration with China Power International Holding Company Limited (CPIHCL) having a 26% stake in the project, which is expected to be increased to 48.5%.

To launch new initiatives, Hubco has formed the following wholly-owned subsidiaries:

- For investing in the imported-coal based 1,320MW power project and other future growth initiatives, the company has incorporated Hub Power Holdings Limited (HPHL). To undertake imported coal-based power project through HPHL, Hubco has set up China Power Hub Generation Company (Private) Limited (CPHGC) with its joint venture partner CPIHCL.
- Hub Power Services Limited, a wholly owned subsidiary, has been incorporated to manage operations & maintenance (O&M) of its existing power assets, its future projects and explore onshore and offshore O&M business opportunities.
- Another wholly-owned subsidiary, Narowal Energy Limited, has taken over the assets and liabilities of Narowal Plant post its demerger under the repealed Companies Ordinance, 1984.
- To set up a 330 MW mine mouth coal power Plant at Thar Coal Block II Sindh, Hubco has established Thar Energy Limited as a wholly-owned subsidiary of Hubco. The company has commenced work on this project.
- The company is also investing US$ 20m in Sindh Engro Coal Mining Company Limited, a joint venture between Hubco, Engro Corporation, Thal Limited, Habib Bank Limited, China Machinery

Engineering Corporation and Government of Sindh, to develop a coal mine at Thar.

Hubco's financial performance is determined by its availability, capacity utilization and plant efficiency. In FY17, load factor of the base plant declined to 65% (FY16: 72%) on account of lower power purchased by National Power Control Center. Finance cost increased due to higher utilization of short term borrowings on account delay in payment from Central Power Purchasing Agency Guarantee Limited. Profit after tax declined due to demerger of Narowal Plant, higher repair & maintenance expenditure on major overhauling at base plant and major maintenance of six engines at Narowal Plant, lower indexation and exchange rate partly offset by higher generation bonus and higher dividend income from subsidiaries. Given lower earnings, Funds from Operations (FFO) also declined in FY17; however, FFO to long term (LT) and total debt improved due to debt repayment. The company enjoys government guaranteed capacity payments till FY27 which will support cash flows. Despite debt repayment, leverage indicators increased in FY17 on account lower equity resulting from Narowal operations being classified as discontinued operations in the financial statements. Gearing and debt leverage were reported at 1.43x (FY16: 1.36x) and 4.90x (FY16: 3.86x) respectively.

In 9MFY18, bottom line of Hubco increased by 9% vis-à-vis same period last year on account of absence of major overhaul and decrease in other expenses although base plant's utilization witnessed decline. Hubco's trade debts have depicted increase in 9MFY18 to Rs. 100.5b (FY17: Rs. 85.6b) on account of continued delay of payments by National Transmission & Dispatch Company. Trade debts are now at the highest level over the last four years. FFO to LT Debt and Total Debt witnessed weakening due to higher short-term borrowings to meet increasing working capital needs on account of rise in overdue receivables. Leverage indicators have further increased due to higher short term borrowing and new long-term loan.

VMFG (Private) Limited
VMFG is an investment holding company with 56.0% interest in HFL. HFL has a moderate business risk profile; the company has been able to sustain gross margins despite increasing competitive operating environment on the back of established market niche of its low end products. Moreover, the company has a low financial risk appetite emanating from its low leveraged capital structure and adequate debt service coverage. However, the company has high concentration in product sales with limited market share in packaged milk segment. As per management, diversification of product range is underway with plans to launch several high margin products.

G4 Mega Pakistan (Private) Limited
G4 has a wholly owned subsidiary named IDBL. In 2017, IDBL acquired entire shareholding of Karachi Properties Investment Company (Private) Limited (KPIC) from previous shareholders; KPIC owns a property known as Hotel Metropole at Club Road, Karachi. Total assets comprise short term investments amounting to Rs. 17.5b; these included TDRs of Rs. 12.1b, mutual funds of Rs. 4.4b and listed equity shares of Rs. 926m. Moreover, the company holds investment property worth Rs. 4.029b (at cost) and Rs. 10.494b (at market value as per valuation report by Anjum Adil and Associates). On the liabilities side, the company has short term borrowing amounting to Rs. 8.1b, long term finance of Rs. 1.9b and interest free loan from associates of Rs. 4.6b which will be repayable on demand.[1] IDBL is in process of construction of a 2.5m square feet mixed use property through an already owned 4-acre plot at the former Metropole Hotel site in Karachi. Recently, IDBL also completed construction and sale of Pakistan's first Leadership in Energy and Environmental Design (LEED) certified commercial office building registering the largest real estate transaction in the country's history.

Strong financial profile of MCPL to support debt repayment
Assessment of financial risk profile derives support from the company's low leveraged capital structure (adjusted for sizeable cash balances & term deposit receipts on a consolidated basis) and adequate debt servicing ability, maintained through stable projected dividend stream from investments, significant cash flow of associated companies and sizeable liquidity on the balance sheet. Moreover, planned restructuring of existing debt on balance sheet will result in sizeable cash accumulation over the rating horizon.

MCPL's standalone income comprises dividend income from its subsidiaries and income from short term investments. During FY18-23, more than 70% of total dividend income is projected to be earned from Hubco, while remaining dividend will be received from VMFG and G4. Historically, Hubco has demonstrated a stable

[1] financial position of G4 is based on statements for the fiscal year ended June 30, 2017

dividend payout. Ongoing expansion projects are expected to result in increasing dividend payouts over the medium to long term although quantum of dividend in the near term may be impacted by sizeable accumulation of receivables due to circular debt and elevated funding requirements for new investments. Management is working on a plan to reduce quantum of trade debts on balance sheet. Moreover, addition of new capacities in the country may result in decline in demand for Hubco's base plant. However, upsurge in tariff project company equity in FY21 till it touches its peak in FY27 (Power Purchase Agreement expiry), US$ denominated and consumer price inflation linked returns would protect dividends.

Balance sheet footing of MCPL stood at Rs. 29.4b (FY17: Rs. 1.2b) at end-9MFY18. Around 4% of total assets are funded by equity while remaining resource base is financed through liabilities (96%). Debt profile of MCPL comprises Term Finance Facility outstanding amounting to Rs. 1.6b at end-9MFY18 and Syndicated Long Term Finance of Rs. 16.6b. Moreover, MCPL's associates and subsidiaries have provided interest fee loans to the company amounting to Rs. 10.0b. Going forward, debt repayment is expected to be supported by healthy projected dividend stream, TDRs worth Rs. 4.7b, cash balances (amounting to Rs. 2.4b at end-9MFY18). Additionally, TDR worth Rs. 4.5b is planned to be transferred from the subsidiary IDBL to MCPL as part of an interest free loan which will further support debt repayment in case of variation in projected dividend income.

Corporate governance framework and management team being enhanced in accordance with envisaged business strategy

Board of directors at MCPL comprises two members including Chief Executive Officer (CEO), who also serves as Chairman of the board. In line with best practices, position of Chairman and CEO should be segregated. A formalized organizational structure exists which is primarily segmented into finance, human resources and investments while an internal audit department is also in place. Going forward, MCPL plans to undertake improvements in corporate governance structure including strengthening of board composition, oversight and management team along with implementation of comprehensive framework for monitoring performance of subsidiaries.

RATING SCALE & DEFINITION

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	Mega Conglomerate (Private) Limited				
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				
	10-July-18	AA-	A-1	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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