RATING REPORT

Ghotki Kandhkot Road & Bridge Company (Pvt.) Limited (GKRBC)

REPORT DATE:
March 15, 2023

RATING ANALYSTS:
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Rating Category	Latest Rating		Previous Rating	
	Long-term	Short-term	Long-term	Short-term
Entity	A	A-2	A	A-2
Rating Outlook	Stable		Stable	
Rating Date	*March 15, 2023*		*November 29, 2021*	
Bank Loan Rating	*AA (blr)*		*AA (blr)*	
BLR Action	*Preliminary*		*Preliminary*	

COMPANY INFORMATION

Incorporated in 2018	**Chief Executive Officer**: Mr. Abdul Karim Qureshi
Private Limited Company	
Key Shareholders (with stake 5% or more):	
Sachal Engineering Works (Pvt.) Limited – 53% Government of Sindh – 47%	

APPLICABLE METHODOLOGY(IES)

VIS Entity Rating Criteria: Industrial Corporates (August 2021)
https://docs.vis.com.pk/docs/CorporateMethodology202108.pdf
VIS Rating Criteria: Toll Roads Rating (August 2020)
https://docs.vis.com.pk/docs/TollRoads202008.pdf

PROFILE

Ghotki Kandhkot Road & Bridge Company (GKRBC) was incorporated as a Private Limited Company in May 2018 to Design, Build, Finance, Operate, and Transfer (DFBOT) two sections of the road located at Ghotki Kandhkot site of Sindh province.

RATING RATIONALE

Project Specifications

The Works and Services Department, Government of Sindh (GoS) in association with the Public Private Partnership Unit in the Finance Department decided to design, construct and develop the project through Public Private Partnership on a Design, Build, Finance, Operate and Transfer (DBFOT) basis. The proposed Bridge over the Indus will connect the National Highway (N-5 at Ghotki) to Indus Highway (N-55 at Kandhkot) along with the project facilities. Both Ghotki and Kandhkot together host the largest oil and gas fields, power projects, crops market, especially rice and fertilizer plants in the country. These districts serve as entry points into Sindh for all traffic coming from the populous up-country and headed for the port city of Karachi. At present, the distance between Kandhkot and Ghotki via Guddu Barrage, the alternate route, is approximately 151 km. Post construction of the 34.7 km (approx.) project, the distance between the two cities will be reduced to 42 km, resulting in significant fuel cost and time savings. Commuter travel time would be reduced by approximately two hours. Moreover, the construction of the bridge is expected to promote industrial and commercial activity and create employment opportunities for the people in that locality.

Salient Features of the Project	
Concession Agreement Date	May 28, 2018
Date of Commencement	July 20, 2020
Expected date of Completion	December 2026
Time Lapsed	28.5 months
Construction period	6 years
Concession period	25 years
Design Consultants	AA Associates (Pvt.) Ltd.
Independent Engineer	Consortium of Loya Associates & Techno-Consult International (Pvt.) Ltd.
Independent Auditor	M/s Riaz Ahmed & Company
EPC Contractor	M/s Sachal Engineering Works (Pvt.) Ltd.
Transaction Advisors	Ernst & Young (EY) – Financial Consultant Loya Associates – Technical Consultant Haider Mota – Legal Consultant

Change in the Scope of the Project

During the rating review period, due to change in design of the project the completion timeline and total project cost increased; however, all other salient features of the project in terms guarantees, equity to debt contribution, EPC contractor, markup rate, shareholding profile and construction & operational risk factors remained unchanged.

The Concession Agreement for the project was signed between Government of Sindh and Ghotki Kandhkot Road & Bridge Company (Pvt.) Limited (GKRBC) (the Concessionaire) on 28th May 2018 for a period of 28 years, out of which construction period was initially decided to be three-years; however, due to change in scope and design of the project, delay in achievement of financial close by GoS and delay in acquisition of land the construction period has increased to 6 years. Based upon the delays and change in scope of project extension in achievement of Financial Close date has been given from 31st January 2022 till 30th June 2023. On the other hand, operations and maintenance period is up to 25 years. At the end of the concession period, the ownership of the project will be transferred to the GoS. GKRBC hired the services of AA Associates (Pvt.) Limited for Survey, Investigation and Design of the Project.

Original Financing Arrangement

Initially the total project cost was estimated at Rs. 14.03b financed through 70% debt and 30% equity. The construction of the project commenced on July 20, 2020 and was financed by the equity of the Concessionaire and GoS; almost all of the equity was utilized by 3rd November 2021 on account of EPC and non-EPC cost.

The equity funding exhausted at a very crucial time and it was imperative for the Project to resume construction works during the upcoming low flood water period in Indus River. Therefore, Sindh Cabinet, decided to extend a Rs. 1.0b short-term debt to the project that was utilized by end-April 2022. Further to resume and expedite the work on the Project a Bridge Finance Facility (*specifications discussed below)* up to 5.0b for a tenor of 12 months was arranged and distributed on 6th July 2022.

Construction of the project was expected to be completed by end-July 2023 as per initially agreed timeline while the financial close was expected to be achieved by end-3QFY22. However, before financial close could be achieved the design of the project was changed by GoS and the 3-Km bridge was replaced by a 12.2-km long bridge in the design. Subsequently, due to the change in the design of the project the cost structure was also revised and is reported higher; the increase is to be financed through the original debt to equity proportion of 70: 30. Both GoS and SEWPL are expected to inject additional equity in proportion of their original equity contributions when required based on the completion status of the project.

The Company was seeking the Syndicated Term Finance Facility (STFF) of Rs. 9.82b for a tenor of around 12 years (inclusive of 2 years grace period) and a Bridge Financing Facility (BF) to the tune of Rs. 5b for a tenure of twelve months. In line with revised project design the STFF amount is expected to increase; however, there are no additional bank guarantee requirements. As per the original indicative term sheet of STFF, security structure entails a Provincial Guarantee in favor of the financiers backed by an unconditional and irrevocable debit authority on the GoS Non-Food Account No. 1 maintained with SBP equivalent to the 50% of the facility amount. The debit authority shall continue at all times over the life of the STFF facility.

Furthermore, a Bridge Financing Facility (BF) to the tune of Rs. 5b for a tenure of twelve months, was required immediately to continue construction works and avoid delay in COD. The security structure of the BF entails a Provincial Guarantee in favor of the financiers backed by an unconditional and irrevocable debit authority on the GoS Non-Food Account No. 1 maintained with SBP equivalent to the 111% of the facility amount. The debit authority shall continue at all times over the life of the BF. The Bridge Facility was to be paid in full either from the proceeds of the STFF or from the Company's own sources. The mark-up rate on the Bridge facility was indicated at 3M KIBOR+115 bps per annum. The original cost and funding specifications are tabulated below:

Funding Type	Amount	Percentage of Contribution
Project Finance	PKR 9,820 Million	70%
Class A Sponsor Equity	PKR 2,244 Million	16%
Class B GoS Equity	PKR 1,964 Million	14%
Total Project Cost	PKR 14,028 Million	100%

Change in Design

Based on the recommendation of Indus River Commission (IRC) it was decided that the original design of the project will be revised and the 3-km Bridge over the River Indus will be replaced with a 12.2-km Bank-to-Bank Bridge. The Project cost in bank-to-bank 12.2 km bridge length is higher than 3 km bridge length by Rs. 3.2b approximately. The difference in upfront project cost may get off-set by significant O&M savings in the river training works for bank-to-bank 12.2 km bridge in the long-run. Furthermore, the bank-to-bank option would pose less probability of damage/destruction in heavy floods as perceived by the IRC. The IRC in the most recent floods of 2022 had observed that bridges that are bank-to-bank over River Indus passed the flood water smoothly without any afflux as compared to bridges that are not bank-to-bank which caused pressure on the flood protective embankments. The expected construction time for the completion of bank-to-bank bridge is around 4 to 5 years.

Revised Financing Arrangement

In accordance with the revised scope of the Project, the total Project cost has increased and is expected to fall between Rs. 33.1b and 34.0b depending upon the final debt amount and S-Curve. As per the revised project cost, GoS additional equity is estimated to be around Rs. 2.7b. Given the Company is only successful in securing additional borrowing of Rs. 5.0b under the "Min Debt Scenario", the differential of additional cost amounting to Rs. 8.3b will be contributed solely by the GoS as additional support funding. As per the Concession Agreement it was already agreed that the additional works (*outside the Project cost)* will be entirely funded and borne by the GoS; the amount is capped at Rs. 15.0b (*Originally: Rs. 12.0b*) in case of 12.2 km Bridge.

However, in case of 'Max Debt Scenario" no additional contribution will be required from GoS but the total cost of the Project will rise due to increase in Financing Cost. Furthermore, additional costs to the Project cost will be funded by debt-to-equity on pro rate basis of 70:30. Concessionaire has agreed to inject additional equity in proportion to its original equity contribution on which it will claim return in virtue of increase in annuity payments. The lenders have agreed to fund minimum additional commercial loan of Rs. 5.0b, however, further negotiations shall be undertaken to lower-down delta funding for GoS. As per the management, the term sheet will be finalized by the end of March'2023. It is important here to note that the Bridge Finance Facility of Rs. 5.0b by HBL and Meezan Bank is expiring in June'2023 and Project Finance Facility has to be available by that time for drawdown to avoid default.

PKR (Million)	Bid Model Cost	Revised Project Cost (Bridge 12.2km)	Revised Project Cost (Bridge 12.2km)
		(Min Debt)	(Max Debt)
EPC Cost	11,290	25,845	25,845
Non-EPC Cost	1,305	2,890	2,890
Financing Costs including Interest during Construction (IDC)	1,433	4,366	5,285
Total Project Cost	**14,028**	**33,101**	**34,020**
Debt	9,820	14,820	23,814
Concessionaire Equity	2,244	5,298	5,443
GoS Equity	1,964	4,634	4,763
Total Equity	**4,208**	**9,932**	**10,206**
GoS Additional Support Funding	**-**	**8,351**	**-**

Current Physical Status of the Project

- The EPC Contractor M/s Sachal Engineering Works (Pvt.) Ltd. has established camps at Ghotki & Kandhkot with well-equipped Laboratories for carrying out quality tests on site and off site for the materials involved in the construction of project.
- At Kandhkot side in the established site camp at KM 25+500, sufficient required machinery and the equipment have been mobilized. Also at Ghotki side; the required earth moving equipment has been mobilized.
- The Section-4 under Land Acquisition Act has been issued in relation to the 4.5 KM (Approx.) long 2-Lane Thull Link Road, 12 KM (Approx.) bridge approach road at Ghotki side and 10 KM (Approx.) bridge approach road at Kandhkot side.
- For 2-Lane Thull Link Road; the site activities are in progress throughout the stretch of 4.5 Km achieving formation of embankment by 98%, sub-grade 94%, sub-base course 94% and Aggregate Base Course 92%.

- Formation of Embankment with River Sand confined on both sides with A4 Soil is in progress at Ghotki Side (Section-I) in the stretch; 0+100~10+400 with physical progress of about 82%, whereas sub grade 76% and sub base course 48%.
- Piling Work done with satisfactory Integrity Testing, construction of Abutment Transoms for Bridges over Jari Wah, Ghota Feeder Canal & Tibbi Minor has been completed. The PSCGs for Jari Wah & Ghota Feeder Bridges and the RCC Beams for Tibbi Minor Bridge have been cast and launched satisfactorily. Deck Slabs along with End Barriers for Jari Wah, Ghota Feeder Canal & Tibbi Minor Bridges have been also cast.
- Bridge Approach Road is in progress for Section-III (KM: 22+500~29+500) at Kandhkot side with physical progress of 84% embankment , sub-grade 70% & sub-base course 49%.
- In Section-II; construction of embankment is in progress for stretch 19+200 to 22+500 with physical progress of 70%.

Key Rating Drivers:

Sponsor Profile: The assigned ratings take into account sound profile of the two shareholders of GKRBC. Shareholding of GKRBC is vested with Sachal Engineering Works (Pvt.) Limited (SEWPL) and Government of Sindh (GoS). SEWPL has 53% equity stake in the project and it holds ordinary Class A voting shares in the company along with the management control; the remaining shareholding (47%) is held by GoS, which has non-voting Class B shares. SEWPL has considerable experience and sound track record in executing infrastructure projects especially toll roads & bridges. Financial profile of SEWPL is also sound.

(Rs. in millions)	FY19	FY20	FY21	FY22
Equity	4,772	4,848	5,718	5,964
Liabilities	2,030	2,279	3,217	4,997
Total Assets	6,752	7,127	8,935	10,961
Revenue	4,097	2,007	4,936	3,824
Operating Profit	841	519	938	474
Net Profit	488	127	588	244
Operating Margin (%)	21%	26%	19%	12%
Net Margin (%)	12%	6%	12%	6%
Leverage	0.42	0.47	0.56	0.84

Demand Risk: Demand risk, associated with uncertainty in future traffic volumes and toll rates, will not be borne by GKRBC as the company will receive fixed annuity payments from the GoS. GKRBC will receive quarterly annuity payments from the GoS. These annuity payments will cover the following components:

- Agreed operations and maintenance expense (including taxes) for that quarter
- Debt payment amount for that quarter (all rental/ interest payments);
- Agreed compensation for equity redemption for that quarter in a manner that 80% of Class A Shares will be redeemed in equal quarterly installments during the operations period (after debt redemption), whereas 20% will be redeemed at the end of Concession Period; and
- Return on equity, calculated in term of agreed Equity IRR of 17% for Sponsors.

Risk of Delay in Annuity Payments: While fixed annuity payments mitigate demand risk for the company, the delay in payment of the same may pose operational challenges for the company as the annuity payments cover both O&M costs and debt payments. However, provisions in the annuity payment agreement ensure that delay risk is also minimal. Annuity payment agreement mandates that the GoS is required to deposit the funds equal to the annuity payment in the annuity payment account 105 days in advance. In case, GoS is unable to deposit the funds by the annuity payment due date, the same shall constitute a GoS event of default. In such a scenario, the GoS is liable to pay the outstanding principal financing provided by the financiers, interest/rental accrued on the debt, termination equity & termination dividend amount.

Cost Overrun Risk: Increase in the prices of escalable raw materials which include cement, bitumen, steel and POL for construction and machinery is an inherent risk in the project. Project costs already incorporate 10% increase in the costs of the escalable items (around Rs. 430m). Concession agreement stipulates that in case the cost of any escalable item exceeds by more than 10%, the GoS shall bear 50% of such escalation cost and the sponsor shall fund the remaining 50% escalation cost. In order to further mitigate cost overrun risk, management of GKRBC has set aside additional Rs. 100m for such contingencies in addition to 10% increase in prices already incorporated in project costs. While construction costs have escalated over the last year, management is confident that the built-in contingency is adequate to absorb the increase in costs. Moreover, saving on Interest During Construction (IDC) given no debt drawdown is expected to provide additional cushion against any cost overrun.

Construction Delay Risk: Both the GKRBC and the GoS have agreed on specific project construction milestones relating to the performance of Construction Works and other obligations to be performed by the Concessionaire until the Project Construction Completion Date. These milestones will have to be achieved as per specific dates mentioned in the construction program. In the event that the concessionaire fails to achieve any project construction milestone within a period of 30 days of the stipulated project milestone date, GKRBC will be liable to pay liquidated damages mandated in the concession agreement to the GoS. Moreover, if the project milestone is not achieved within 90 days of the Project Milestone Date, the same will constitute a concessionaire event of default and the government has the right to terminate the concession agreement. Similarly, GKRBC will also be liable to pay liquidated damages to GoS in case it fails to achieve Substantial Completion by the Scheduled Substantial Completion Date (36 months from Project commencement date). While financial close of the project has been delayed due to revision in the scope of the project, the construction commenced as per plan in July'20 through upfront equity injection by the sponsors. Consequently, the timelines of the project are on track except few minor delays due to revision in design and flooding in River Indus and is expected to be completed on time.

Debt Servicing: As per the new estimates, for the purpose of raising debt GKRBC will be drawing a STFF amounting between Rs. 14.8b and Rs. 23.8b. Following are some key features of the security:

- Pricing @ 3M KIBOR+1.3% based on robust security arrangement;
- Stretched tenor of the facility of 2 plus 10 years;
- Security structure encompassing Provincial Guarantee in favor of the financiers backed by an unconditional and irrevocable debit authority on the GoS Non-Food Account No. 1 maintained with SBP equivalent for 50% of the facility amount.

The principal will be redeemed in 40 equal quarterly installments. Given that debt payments are covered under annuity payments, cushion in debt servicing is adequate. Moreover, till the attainment of the project finance facility, an interim bridge financing facility is being utilized to the tune of Rs. 5b in order to continue with works on the Project. Upon issuance of the project finance, bridge financing will be settled. The amount raised by STFF might vary depending upon the final agreement with the lenders.

Annuity Payments

Quarterly annuity payments received from the GoS will be sole source of revenue for GKRBC. The annuity payments/revenue of GKRBC will be routed through the designated collection accounts held under lien by the banks. The annuity payments will include four major components including O&M costs and debt payments. The two major maintenance overhaul expenses will be incurred in the 11th and 21st year of operations are not covered under the annuity payments to be received by GKRBC. GKRBC will acquire grants from the GoS in the 11th and 21st year to incur major maintenance expense. Given that debt payments are included in the annuity payments, DSCR of the company will remain adequate throughout the life of the project.

ISSUE/ISSUER RATING SCALE & DEFINITION Appendix I

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.

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<tr><td>Sector</td><td>Toll Roads</td></tr>
<tr><td>Type of Relationship</td><td>Solicited</td></tr>
<tr><td>Purpose of Rating</td><td>Entity & Debt Rating</td></tr>
<tr><td>Rating History</td><td>
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<tr><th>Rating Date</th><th>Medium to Long Term</th><th>Short Term</th><th>Rating Outlook</th><th>Rating Action</th></tr>
<tr><td colspan="5">RATING TYPE: Entity</td></tr>
<tr><td>15/03/2023</td><td>A</td><td>A-2</td><td>Stable</td><td>Reaffirmed</td></tr>
<tr><td>29/11/2021</td><td>A</td><td>A-2</td><td>Stable</td><td>Reaffirmed</td></tr>
<tr><td>23/10/2020</td><td>A</td><td>A-2</td><td>Stable</td><td>Initial</td></tr>
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<tr><td>Statement by the Rating Team</td><td>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.</td></tr>
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<tr><td>Due Diligence Meetings Conducted</td><td>
<table>
<tr><th>Sr. No</th><th>Name</th><th>Designation</th><th>Date</th></tr>
<tr><td>1</td><td>Mr. Fuad Kehar</td><td>Executive Director- Financial Unit</td><td>December 19, 2022</td></tr>
<tr><td>2</td><td>Zafar Bhakhtiari</td><td>Executive Director- Financial Unit</td><td>December 19, 2022</td></tr>
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