RATING REPORT

Lahore Sialkot Motorway Infrastructure Management (Private) Limited (LSMIM)

REPORT DATE:
August 19, 2020

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-2	A-	A-2
Rating Outlook	Stable		Stable	
Rating Date	*August 19, 2020*		*March 11, 2019*	

COMPANY INFORMATION	
Incorporated in 2016	**Chief Executive Officer**: Brig. Atif Majeed
Private Limited Company	**Chairman:** Major General Kamal Azfar
Key Shareholders (with stake 5% or more):	**External Auditor:** Deloitte Yousuf Adil, Chartered Accountants
Frontier Works Organization - 21% (Class 'A' Shares)	
National Highway Authority - 79% (Class 'B' Shares)	

APPLICABLE METHODOLOGY(IES)
VIS Entity Rating Criteria: Industrial Corporates (May 2019) **https://www.vis.com.pk/kc-meth.aspx**
VIS Rating Criteria: Toll Roads Rating (November 2018) **https://www.vis.com.pk/kc-meth.aspx**

Lahore Sialkot Motorway Infrastructure Management (Private) Limited (LSMIM)

PROFILE

LSMIM was incorporated as a private limited company in 2016. The company is formed for the purpose of construction, collecting toll and operation and maintenance of Lahore Sialkot Motorway. Sponsors of the company include National Highway Authority (NHA) and Frontier Works Organization (FWO).

RATING RATIONALE

The ratings assigned to Lahore Sialkot Motorway Infrastructure Management (Private) Limited (LSMIM) takes into account strong sponsorship profile of its two shareholders. Shareholding of the company is vested with Frontier Works Organization (FWO) (Class A shares) and National Highway Authority (NHA) (Class B shares), having ample experience in infrastructure projects. FWO has undertaken major projects under public private partnership (PPP) and Build-Operate-Transfer (BOT) mandates. The ratings draw comfort from precise financial planning and execution resulting in avoidance of cost overruns.

LSMIM is a Special Project Company (SPC) with registered office based in Rawalpindi, Punjab. The company has entered into a concession agreement for a period of 25 years with NHA for construction, management and maintenance of the Lahore Sialkot Motorway (LSM). The project is established under the Public Private Partnership (PPP) regime on BOT basis, with FWO. Under the agreement, LSMIM as concessionaire is responsible for construction as well as operations and maintenance. LSMIM has employed FWO as EPC Contractor and O&M Contractor.

The motorway is operational since March 18, 2020. Due to non-availability of concession area, some additional works are pending including construction of Sambrial Interchange, which are envisaged to be completed by end-October'20. However, temporary arrangements to facilitate commuters' journey have been provided. Therefore, the construction and implementation risks are largely addressed. Commercial Operation Date (COD) is expected to be achieved on October 30, 2020.

Rating Drivers

Capitalization and debt servicing: NHA has injected its equity amounting Rs. 18b and subordinated loan amounting Rs. 5b at the inception of the project; shares against equity has been issued in subsequent periods. Ratings also draw comfort from terms of the subordinated loan from NHA where repayment is to be made from the 11th year of the concession agreement. FWO has injected equity of Rs. 6.8b so far, out of which shares have not been issued against Rs. 2.1b; remaining equity of Rs. 418.6m will be injected for next EPC payment. Loan drawdown against the Syndicated Term Finance Facility (STFF) of Rs. 12b amounted to Rs. 8.8b at end-FY20; the company has applied for the extension of debt availability period *(availability period expired on March 31, 2020)*, meanwhile, in case of non-extension, equivalent financing of Rs. 3.2b will be provided by FWO in the form of subordinated loan. As per agreement, any other shortfall in project financing will also be provided by FWO in the form of equity or subordinated loan. Total EPC payments to be made amounted to Rs. 41.1b, against which Rs. 37.4b have been paid so far, while the remaining payment is needed to be funded through unavailed debt facility or through funds provided by FWO. As the loan amount is drawdown against due EPC invoices, which in turn are generated against actual milestones achieved, interruption in land acquisition by NHA has resulted in delayed generation of invoices and thus leading to deferment in drawing loan facility.

The assigned ratings also incorporate the presence of Debt Service Reserve Account (DSRA) with an amount equal to next debt repayment installment to be maintained at all times after termination of grace period. This mechanism has been built as part of the overall project cost. Debt repayment capacity is contingent upon realization of project traffic volumes. Given relief by GoP for Covid'19 and very low traffic volumes, the management has applied for rescheduling of first and second installments *(due on June 20, 2020 and December 20, 2020)* for one year, which is pending approval.

Meanwhile, as per management, the company has also applied for extension of grace period till October 30, 2020. DSRA is not funded yet and is deferred till the outcome of negotiations regarding extension of grace period and loan installment deferment with the agent bank. LSMIM has to maintain minimum Debt Service Coverage Ratio (DSCR) of 1.2x and target DSCR is 1.5x.

Revenues have fallen short of projected growth amidst lockdown: Operational toll rates have been applied and an increase in toll collection has been noted since the motorway became fully operational; albeit, traffic volume data witnessed a notable shortfall from projected volumes due to impact of pandemic. Toll collection amounted to Rs. 137.8m during 2HFY20. Monthly toll collection and traffic volume from January 2020 to July 2020 is tabulated below:

	Jan'20	Feb'20	Mar'20	Apr'20	May'20	Jun'20	Jul'20
Monthly Toll Revenue (in Rs.)	2,003,820	4,446,260	15,251,140	27,724,520	44,036,130	44,384,420	52,986,690
Total Traffic Volume	53,928	121,285	184,094	264,527	410,325	424,348	490,961

The management expects an increase in toll collection after overall relaxation in lockdown. With higher profitability, Funds from Operations (FFO) is expected to increase steadily over the years. Liquidity profile draws support from projected growth in revenues.

Traffic mix indicates that majority of the volume on the proposed route is commuter related. By using LSM, the commuters will save approximately 1.25 hours in travel time and some saving in fuel cost in comparison to the travel via the alternate route (Grand Trunk (GT) Road). Higher time taken and fuel costs over the alternate route are a function of greater distance. Since time and cost savings are sizeable, traffic volumes are expected to be sustainable. Traffic survey study also indicates high willingness to pay toll by the consumers. Moreover, if NHA or any other public-sector entity decides to establish a competing route, then it will be ensured that the competing route shall be tolled at least equivalent to an amount 1.5 times higher than prevailing toll rates imposed at LSM. Otherwise, LSMIM is entitled to receive losses in toll revenues from NHA. Furthermore, in case of extraordinary circumstances, which are beyond reasonable control, the company is entitled to claim shortfall in revenue or complete loss of revenue under *Force Majeure* clause of concession agreement.

Revenue risk related to toll rates remains largely addressed: Toll revenues will also be a function of increase in toll rates as mandated in the concession agreement. Toll rates will be revised upwards by 8% every year. In case, the stipulated increase in toll rates is not implemented or any downward revision in toll rates, LSMIM is liable to receive compensation from NHA for the loss in revenues. Apart from tolls, growth in revenues from other sources (service area) is expected; however, its proportion is expected to remain small.

Lahore Sialkot Motorway Infrastructure Management (Pvt.) Ltd. Appendix I

BALANCE SHEET *(in PKR millions)*	FY18	FY19
Concession Work in Progress	14,324.2	26,774.7
Mobilization Advance	11,061.5	8,242.1
Secured Advance	2,739.2	2,086.3
Cash and Bank Balances	1,967.0	45.6
Other Assets	182.8	214.6
Total Assets	30,274.7	37,363.3
Long Term Loan (including current maturity)	2,003.4	4,181.0
Subordinated loans	5,202.1	5,513.4
Tarde and Other Payables	337.6	4,901.7
Total/Tier-1 Equity	22,731.4	22,767.1
Paid-up Capital	21,643.3	22,765.8
INCOME STATEMENT	**FY18**	**FY19**
Net Sales	-	-
Gross Profit / (Loss)	-	-
Profit / (Loss) Before Tax	(46.1)	47.9
Profit After Tax	(42.0)	35.7
Funds from Operations (FFO)	-	-
RATIO ANALYSIS	**FY18**	**FY19**
Gross Margin (%)	-	-
Net Margin (%)	-	-
Current Ratio (x)	47.2	2.2
Net Working Capital	1,5603.3	5,681.3
FFO to Total Debt (x)	-	-
FFO to Long Term Debt	-	-
Debt Leverage (x)	0.33	0.64
Gearing (x)	0.32	0.43
DSCR (x)	-	-
ROAA (x)	-	0.1
ROAE (x)	-	0.2

ISSUE/ISSUER RATING SCALE & DEFINITIONS Appendix 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 — Appendix III

Name of Rated Entity	Lahore Sialkot Motorway Infrastructure Management (Private) Limited (LSMIM)
Sector	Toll Roads
Type of Relationship	Solicited
Purpose of Rating	Entity rating
Rating History	see table below
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.

Rating History

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
RATING TYPE: ENTITY				
19/08/2020	A-	A-2	Stable	Reaffirmed
11/03/2019	A-	A-2	Stable	Initial

Due Diligence Meetings Conducted

	Name	Designation	Date
1	Mr. Bilal Qureshi	Deputy Manager Finance & Accounts	July 3, 2020