RATING REPORT

Indus Wind Energy Limited

REPORT DATE:
September 10, 2024

RATINGANALYSTS:
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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 Date	September 10, 2024		August 07, 2023	
Outlook/RW	Stable		Stable	
Rating Action	Reaffirmed		Reaffirmed	

COMPANY INFORMATION	
Incorporated in 2015	**External auditors:** Yousuf Adil, Chartered Accountants
Public Limited (Unlisted) Company	**Chairman:** Mian Naveed Ahmad **CEO:** Mian Shahzad Ahmed
Key Shareholders (with stake 5% or more): *Indus Dyeing & Manufacturing Company Limited (the Parent Company) - 99.99%*	

APPLICABLE METHODOLOGY(IES)
VIS Entity Rating Criteria Methodology – Corporates https://docs.vis.com.pk/docs/CorporateMethodology.pdf

RATING SCALE(S)
VIS Issue/Issuer Rating Scale: https://docs.vis.com.pk/docs/VISRatingScales.pdf

Indus Wind Energy Limited

OVERVIEW OF THE INSTITUTION

IWEL was incorporated as a Public Limited Company on February 4, 2015 under the repealed Companies Ordinance, 1984 (now Companies Act, 2017). The windfarm is located in Deh Kohistan, 7/3 & 7/4 Tapo Jungshahi Taluka & District Thatta. The registered office of the company is located at Office # 508, Beaumont Plaza, Beaumont Road, Civil Lines Quarters, Karachi.

Profile of Chairman

Mian Naveed Ahmad has done B.Sc. Accounts from North Carolina State University, Raleigh, NC, USA. He has been associated with the Indus group for more than two decades.

Profile of CEO

Mian Shahzad Ahmed is also CEO of Indus Dyeing & Manufacturing Company Limited. He has done BBA Marketing from Syracuse University, New York, USA. He has around 30 years of experience of actively managing and monitoring the parent company.

RATING RATIONALE

Corporate Profile

Indus Wind Energy Limited ('IWEL' or 'the Company') was incorporated as a public unlisted company on February 04, 2015 and is a wholly-owned subsidiary of Indus Dyeing & Manufacturing Company Limited (IDMCL). IWEL is primarily engaged in the production and sale of electricity through its 50MW wind-power plant located at Deh Kohistan, District Thatta, Sindh. The head office is located at Civil Lines Quarters, Karachi.

Project Design

The project comprises 25 WTGs of General Electric Inc. (GE), with the nameplate capacity of 2MW of each turbine, having total net capacity of 50 MW. The Company also acquired GE Power & Water wind plant Supervisory Control and Data Acquisition (SCADA) system. Furthermore, a dedicated remote data connection to a wind farm network has been deployed for the GE's Customer Support Center (CSC) to monitor and perform remote operations; the Company is responsible for the availability and reliability of the remote connection.

The Company signed an Implementation Agreement (IA) with the Government of Pakistan (GoP), represented through the Alternative Energy Development Board (AEDB) on November 12, 2019. The Company was allocated land of 428 acres by the Government of Sindh in Jhimpir, Thatta through a lease agreement in May 2017 and Generation License was granted in August 2017 by the National Electric Power Regulatory Authority (NEPRA).

The project cost was estimated in the Tariff determination dated November 19, 2018 by NEPRA with cost outlay of USD 64.07m, financed through debt to equity mix of 80:20. Half of the debt component comprised local borrowing through the SBP's concessionary refinancing scheme for renewable energy projects while the other half pertained to a foreign loan from British International Investment Plc (BII).

The "Construction Contract" was signed with Hydrochina International Engineering Company Limited (HIECL) as onshore construction contractor and the "Equipment Supply Contract" with Hangzhou Huachen Electrical Power Control Co. Limited (HHEPCCL) as offshore supplier. HIECL is a subsidiary of 'Powerchina', one of the biggest construction groups in the power sector with engagement in over 100 countries.

HIECL is also the O&M contractor for the initial warranty period of 2 years after the COD while the Company has entered into a long-term O&M contract with GE for the 11 years starting after the completion of warranty period; post-March'24, the new O&M contract with GE has come into effect. As per the O&M contract, at least 97% plant availability will be guaranteed; failure to comply with the benchmark will result in payment of liquidity damages by the contractor to the Company up to 50% of the annual agreement price. The Company has adequate insurance coverage for cargo, operations, erection, liability, third party and terrorism. The Company started construction eight months after the financial close, in July'20, as the government scheduled the availability of grid by end-Dec'21. Owing to Covid-19 related disruptions the grid was made available to the Company in Jan'22. As per management, 3 months delay in project outlay led to $5.5m losses claimed by IWEL whereas $6.0m in losses were claimed by HIECL. However, the claims were mutually settled without any payment made by any of the parties. The project achieved commercial operations on March 25, 2022.

EPA

The Company entered into a 25-year long Energy Purchase Agreement (EPA) with 'take or pay' provision on November 09, 2019, with the Central Power Purchasing Agency (Guarantee) Limited (CPPA-G). As per the EPA, the benchmark annual generation amounts to 166,440 MWh with a corresponding net annual capacity factor of 38%.

NEPRA issued tariff determination for IWEL on November 18, 2018. The cost-plus levelized tariff for the concession period is 5.7517 Rupees/kWh or 4.7931 US Cents/kWh. The reference tariff was determined based on interest cost of 6% with ten-year repayment period and reference exchange rate of Rs. 120/USD. The Company applied for one-time true-up adjustment of the reference tariff rates in Dec'22; however, as per management, decision by NEPRA regarding the same is awaited. Nonetheless, the Company also applied for interim relief to raise the tariff rate based on quarterly indexation of the revised local and US Consumer Price Index (CPI), PKR/USD exchange rates and LIBOR rate for the period March'22 to June'23. During May'23, NEPRA granted indexation for the same for March'22 onwards.

Moreover, energy production in excess of the 38% net annual plant capacity factor benchmark will result in the following tariffs:

Net Annual Plant Capacity factor	% of Prevalent Tariff Allowed to Power Producer
Above 38% up to 40%	5%
Above 40% up to 42%	10%
Above 42% up to 44%	20%
Above 44% up to 46%	40%
Above 46% up to 48%	80%
Above 48%	100%

The long-term nature of the EPA with the CPPA-G mitigates offtake risk as well as default risk pertaining to receivables from the same. Additionally, the indexation of the tariff rate, additional return for excess energy production and the partial compensation of Non-Project Missed Volumes (NPMV) on account of Non-Project Events (NPE) provides comfort in terms of revenue stability and profitability metrics.

Operational Performance

The Company has successfully completed two full years of operations. However, capacity factor fell below the stipulated 38% requirement outlined in the EPA during FY23 on account of curtailments by the National Transmission & Dispatch Company (NTDC) due to availability of cheaper power sources over the winter period; however, revenue impact of the same was partially mitigated due to compensation of NPMV, as per management. Nonetheless, an uptick in power generation was exhibited during 9MFY24 due to fewer curtailment events and availability of wind resource. Additionally, plant availability has been maintained above the 97% benchmark over the rating review period, as per the management. Breakdown of operational performance can be seen below:

	FY22*	FY23	9MFY24
Capacity Factor (%)	65.1%	34.7%	37.9%
Output (KWh)	76,600	151,860	124,750

**Represents March-June'22*

<u>Key Rating Drivers</u>

Business Risk

VIS categorizes the overall risk profile of the renewable power generation sector as medium-to-low. The industry's high capital requirement, complex regulatory framework and technology risk pose significant barriers to entry. Wind power projects (WPPs), in particular, have repeatedly faced curtailment events by the government on account of insufficient transmission and distribution infrastructure which as hampered energy production. Additionally, WPPs are subject to wind risk due to varying weather conditions; however, completion of an extensive wind study by external consultants reflects limited potential risk to the operations of IWEL.

The overall power demand is closely driven by population growth, urbanization rate, lifestyle preferences, and industrial activity. During 9MFY24, out of the 68,559 GWh of electricity consumed (9MFY23: 69,247 GWh, FY23: 112,891 GWh), about 49.2% (9MFY23: 48.1%, FY23: 47.4%) emanated from households followed by industries at 26.3% (9MFY23: 28.3%, FY23: 27.5%). While deterioration in macroeconomic conditions and soaring tariff prices over the rating review period have impacted industrial activity, household demand is expected to remain stable given the inelastic nature of individual power consumption and the rising population.

Moreover, government targets for expansion of the renewable energy sector are ambitious. The Alternative Renewable Energy (ARE) Policy 2019 aims for 30% of total generation capacity to come from renewable sources (excluding hydel power) by 2030, while the Integrated Generation Capacity and Expansion Plan 2022 (IGCEP) targets increasing the share of renewable energy (including hydel power) from 33% to 62% by 2031. Despite these goals, by end-March'24, renewable energy sources contributed only 6.8% to the total installed electricity capacity of 42,131 MW and just 4.3% to the total electricity generation of 92,091 GWh. Furthermore, only two wind power projects (WPPs), with a combined capacity of 100 MW, are currently under development. These projects are expected to achieve commercial operation by June'28 which would bring the total number of wind power projects to 38.

Sponsors Profile

The ratings reflect the Company's affiliation with the 'Indus Group of Companies,' a prominent entity within the textile industry. The group includes IWEL's parent company, Indus Dyeing & Manufacturing Company Ltd. as well as Indus Lyallpur Ltd., Sunrays Textile Mills Ltd., and Indus Home Ltd. Collectively, the group operates four cotton ginning factories, five yarn spinning mills, and one of the country's largest terry towel manufacturing facilities.

Additionally, demonstrated sponsor support in the form of short-term loans by the parent company is viewed positively; the same were utilized to finance onshore EPC cost.

Profitability

Following completion of a full year of commercial operations, IWEL posted a topline of Rs. 2.1b (FY22: Rs. 850.8m) during FY23 which comprised almost exclusively of energy purchase price (EPP). The same also includes Rs. 199.8m (FY22: Rs. 271.3m) pertaining to one-time adjustment of the reference tariff by NEPRA. The gross margin level was high at 61.2% (FY22: 74%) on account of indexation of tariff rate. However, the sizeable financing cost of Rs. 809.4m (FY22: Rs. 141.9m) due to a rise in local and international interest rates which resulted in pressure on net margins which stood at 15.7% (FY22: 49%) in FY23. Moreover, the overall decline in margins vis-à-vis FY22 is also due to the impact of higher operational and depreciation expenses following a full year of operations.

During 9MFY24, the Company's net revenue exhibited an uptick on the back of increased energy output coupled with tariff adjustments. The gross margin level remained high at 60.4%; a slight decrease in the same is due to lag in tariff revision. Nonetheless, net margin exhibited a notable increase to 21% mainly owing to an increase in other income to Rs. 60.4m (FY23: Rs. 24.6m) on account of profit on bank deposits in line with the high local policy rate environment. Going forward, profitability is expected to remain satisfactory, supported by tariff indexation, provided that unexpected curtailment events do not hamper offtake.

Capitalization

The Company's equity base expanded over the rating review period to Rs. 3.2b (FY23: Rs. 2.8b, FY22: Rs. 2.5b) by end-March'24 in conjunction with profit retention. The overall debt profile comprised exclusively of long-term borrowings at end-March'24, amounting to Rs. 9.9b (FY23: Rs. 10.8b, FY22: Rs. 9.4b). About 65.7% of the same pertained to foreign financing from British International Investment (formerly CDC Group UK) which carries markup at a rate of 3M LIBOR plus 4.25% per annum with a tenor of 13 years. The remaining long-term borrowings constitute majorly of concessionary local financing obtained at the SBP rate plus 1.75% per annum under the SBP's renewable energy financing facility. IWEL also recorded Rs. 27.8m in finance lease liabilities (FY23: Rs. 30.3m, FY22: Rs. 31.1m) pertaining to the development of the wind power plant and the Company's registered office.

Short-term loans were extended by the parent company since FY20 solely to finance the sales tax portion of the onshore EPC cost. The facility had a markup at the parent company's average borrowing rate and was payable on demand after achievement of COD. Full repayment of the same was completed during FY23. Moreover, given that working capital needs were met entirely through internal capital during 9MFY24, short-term borrowings were nil (FY23: Rs. 130m, FY22: Rs. 241.1m). While the management does not project need for short-term financing in the foreseeable future, the Company maintains a working capital finance facility of Rs. 1b which carries a markup of 1M KIBOR + 1.5% per annum.

Despite improvement in gearing and leverage levels over the rating review period due to expansion of equity base and timely repayment of long-term financing, the same remained elevated at 3.09x and 3.17x, respectively (FY23: 3.84x, 3.94x; FY22: 3.75x, 4.13x), exposing the Company to financial risk. Nonetheless, the same is projected to moderate over the rating horizon in line with continued debt repayments and profit retention given continued efficient operations of the plant.

Liquidity

The Company's liquidity profile is considered adequate with a current ratio of 1.18x at end-9MFY24 (FY23: 1.01x, FY22: 0.9x); timeline improvement in the same is largely attributable to repayment of trade payables to the EPC contractor. Trade debts amounted to Rs. 583m (FY23: Rs. 1.1b, FY22: Rs. 726.4m) at end-March'24; the associated default risk is considered minimal given that the same are due solely from the CPPA-G which are secured by sovereign guarantee. Additionally, receivables are due on or before thirty days following the date of receipt on invoices by the CPPA-G and delayed payment are subject to interest at the rate of KIBOR plus 2%, in accordance with the EPA. As per management, the Company has experienced clearance of receivables largely on a timely basis which has resulted in an improvement in its cash conversion cycle during 9MFY24. Going forward, timely clearance of receivables will be an important rating consideration.

Coverages

The Funds from Operations (FFO) exhibited an uptick over the rating review period on an annualized basis in line with enhanced profitability, amounting to Rs. 753.7m during 9MFY24 (FY23: Rs. 833.4m, FY22: Rs. 314.3m). Consequently, debt service coverage ratio (DSCR) improved to 1.1x (FY23: 0.98x, FY22: 0.52x). Although cash flow coverage increased as well, it remained constrained due to sizeable debt levels, with FFO-to-total debt at 0.1x (FY23: 0.08x, FY22: 0.03x).

REGULATORY DISCLOSURES					Appendix I
Name of Rated Entity	Indus Wind Energy 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				
	09/10/2024	**A**	**A-2**	**Stable**	**Reaffirmed**
	08/07/2023	A	A-2	Stable	Reaffirmed
	05/16/2022	A	A-2	Stable	Reaffirmed
	03/19/2021	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.				
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.				
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Due Diligence Meetings Conducted		**Name**	**Designation**	**Date**	
	1	Saleem Bandukda	COO	21 August 2024	
	2	Hassaan Ahmed	Manager Finance	21 August 2024	