RATING REPORT

Gujranwala Electric Power Company Limited

REPORT DATE

November 07, 2024

RATING ANALYSTS:

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RATING DETAILS

Rating Category	Initial Rating	
	Long-term	Short-term
Entity	AA-	A1
Rating Date	*November 07, 2024*	
Rating Outlook/Rating Watch	Stable	
Rating Action	Initial	

COMPANY INFORMATION

Incorporated in 1998	**External auditors:** Grant Thornton Anjum Rahman & Co. Chartered Accountants
Public Unlisted Company	**Chief Executive Officer (CEO):** Mr. Muhammad Ayub
Key Shareholders (with stake 5% or more):	**Chairperson:** Mr. Imran Zaffar
President of Islamic Republic of Pakistan ~ 99.6%	

APPLICABLE METHODOLOGY(IES)

***Applicable Rating Criteria: Corporates*:**
https://docs.vis.com.pk/docs/CorporateMethodology.pdf

APPLICABLE RATING SCALE(S)

VIS Issue/Issuer Rating Scale:
https://docs.vis.com.pk/docs/VISRatingScales.pdf

Gujranwala Electric Power Company Limited

OVERVIEW OF THE INSTITUTION	RATNG RATIONALE

Gujranwala Electric Power Co. Ltd. *was established in 1977 as Area Electricity Board Gujranwala, under the umbrella of WAPDA. In 1998, established as Distribution Company "GEPCO" under administrative control of PEPCO after dis-bundling of WAPDA.*

Company Profile:

Gujranwala Electric Power Company Limited ('GEPCO' or 'the Company') is an unlisted public limited entity incorporated in Pakistan. Established on April 2, 1998, and commencing commercial operations on July 1, 1998, GEPCO took over the assets, liabilities, and obligations of the Gujranwala Area Electricity Board, previously owned by Water and Development Authority ('WAPDA'). The Company's primary function is electricity distribution within its defined geographical territory, including Gujranwala, Sialkot, Narowal, Gujrat, Mandi Bahauddin, and Hafiz Abad. The registered office is located at Model Town, GT Road, Gujranwala. GEPCO is primarily sponsored by the Government of Pakistan ('GoP'), with 99.6% of the shares held by the President of the Islamic Republic of Pakistan.

Board Of Directors:

The current Board of Directors (BoD) was appointed in August 2024. The BoD consists of nine members, including five independent directors, one of whom is a female representative. The board is chaired by Mr. Imran Zafar and comprises members with an average of 30 years of industry-specific experience.

Senior Management:

The management team comprises professionals with diverse expertise in engineering, economics, accounting, commerce, and electrical engineering. The team includes individuals with advanced academic qualifications, such as master's degrees in engineering, economics, accounting, and chartered accountancy, obtained from recognized institutions. Members bring extensive experience across various geographical regions and operational sectors.

Enterprise Resource Planning (ERP) Framework:

The Company initiated the implementation of the ERP project in 2019, incorporating multiple modules, including Financial Accounting & Controlling (FICO), Human Capital Management (HCM), Materials Management (MM), and Project Systems (PS). Oracle is utilized for billing operations, whereas SAP HANA is employed for other operational functions.

Internal Control Framework

The Company's internal control framework is structured to incorporate oversight from various Board committees, including the Audit, Human Resource, Strategy and Finance, Enterprise Risk, Procurement, and Nomination Committees. Each committee comprises members with relevant expertise, and their roles and responsibilities are outlined in their respective Terms of Reference. The framework provides oversight of financial, operational, and strategic functions, facilitating governance and risk management. Regular meetings and active participation by committee members support the Company's adherence to governance standards and regulatory compliance, maintaining continuity in these processes from the prior period.

Market Implementation & Regulatory Affairs Department (MIRAD)

In line with Competitive Trading and Bilateral Contracting Market (CTBCM) and National Electricity Policy, which envisage power market liberalization, GEPCO has established MIRAD to act as interface between the CTBCM and the GEPCO by undertaking multidimensional corporate strategy functions. The functions include demand forecasting, transmission facility planning, bilateral contracting, contract management, financial analysis, legal reviews and regulatory affairs / compliance. The MIRAD is manned with an adequate number of qualified and experienced professional to undertake the entrusted roles. The MIRAD maintains concurrent liaison with Regulator (NEPRA) and coordination with other X-WAPDA DISCOs and K-Electric in leading on multiple common tasks, e.g. Combined Power Acquisition Program and determination of Use of System Charges for open access users etc.

Industry Overview:

Pakistan's power sector operates under a centralized model, where the Central Power Purchasing Agency Guarantee (CPPA-G) acts as the sole purchaser of electricity for ten distribution companies (DISCOs). DISCOs are responsible for electricity distribution to end consumers, infrastructure management, billing, and collections.

DISCOs provide demand forecasts to CPPA-G, which procures power from generation companies (GENCOs) and Independent Power Producers (IPPs). The National Electric Power Regulatory Authority (NEPRA) regulates procurement and pricing mechanisms, setting tariffs based on generation, transmission, and distribution costs, while the government implements a largely uniform tariff across all DISCOs to maintain which the government provides subsidies to the DISCOs.

The sector faces structural challenges, particularly the accumulation of circular debt. Efforts to reduce this and enhance efficiency include plans for privatization, improved management of DISCOs, the introduction of Advanced Metering Infrastructure (AMI), and installation of Aerial Bundled Cables (ABC) to reduce illegal connections and line losses.

Operational Performance:

Categorization Of Sales (GWh)	FY21	FY22	FY23	FY24
Domestic	58.3%	59.1%	58.3%	59.6%
Commercial	6.2%	6.6%	6.7%	6.9%
Industrial	25.4%	24.3%	24.2%	23.3%
Agriculture	5.0%	4.6%	5.0%	4.4%
Bulk	1.5%	1.5%	1.5%	1.5%
Public Light	0.1%	0.1%	0.2%	0.1%
Others	3.6%	3.7%	4.1%	4.2%
Total	**100.0%**	**100.0%**	**100.0%**	**100.0%**

The sales categorization data from FY21 to FY24 reflects stability across primary consumer segments. Domestic consumption continues as the largest contributor, maintaining a consistent share, indicative of steady residential electricity demand. The commercial segment exhibits incremental growth, correlating with increased business activities in the service sector. Industrial consumption, while overall stable, has experienced a marginal decline, mirroring broader economic conditions. Agricultural demand has shown minor fluctuations, maintaining a share between 4.5-

5.0% of total offtake. The bulk and public lighting segments have remained stable with limited impact on overall sales. The "Others" category recorded a modest increase, indicating a slight rise in demand from non-core segments.

	FY21	FY22	FY23	FY24
Distribution Losses (GWh)	8.4%	8.2%	8.1%	10.8%

In FY24, distribution losses increased due to transmission inefficiencies, aging infrastructure, delays in meter readings, inaccuracies in meter readings, and challenges in managing higher demand loads. In response, the Company's management has engaged an independent third party, Pakistan Powers International (PPI), to audit and assess the technical losses as part of its corrective measures.

Revenue Components:

Distribution of electricity: The Company generates the majority of its revenue through the sale of electricity to consumers within designated regions. GEPCO has established three Power Purchase Agreements ('PPAs') with Marala, Chianwali, and CPPA. Under these agreements, GEPCO procures electricity from these entities and distributes it to end consumers. This segment has maintained a 3-year average consistent revenue contribution of approximately 92.4%.

Subsidies from GoP: The Company receives subsidies from GoP to support the discounted sale of electricity to low-income populations. These subsidies encompass various components, including the Tariff Differential Subsidy, AQTA Subsidy, Zero Rated Industrial Rebate, and Kissan Package Subsidy Income. Over the past three fiscal years, this revenue segment has consistently contributed approximately 7.6% on average to the Company's total revenue.

Clientele:

No. Of Consumers	FY21	FY22	FY23	FY24
Domestic	86.1%	86.3%	86.6%	87.1%
Commercial	10.0%	9.9%	9.6%	9.3%
Industrial	1.9%	1.9%	1.9%	1.8%
Agriculture	1.3%	1.3%	1.3%	1.2%
Bulk	0.0%	0.0%	0.0%	0.0%
Public Light	0.0%	0.0%	0.0%	0.0%
Others	0.5%	0.5%	0.5%	0.5%
Total	**100.0%**	**100.0%**	**100.0%**	**100.0%**

Key Rating Drivers:

Low business risk profile

The assessment of the Company's business risk profile highlights that a significant portion of transactions are conducted with government entities, financially stable banks, and customers from whom security deposits are held. This, coupled with the disconnection threat, results in a low to medium credit risk profile. Liquidity risk on the balance sheet is low in terms of timing buckets; however, timing variations in collections may introduce some liquidity risk exposure. Pricing risk remains low due to the monopoly market structure and regulated pricing. Currency risk is mitigated through foreign exchange cover on FX liabilities, while interest rate risk is addressed through a time-delayed tariff adjustment determined by the government.

Strategic importance of GEPCO as a power utility further supports business risk profile

The assigned ratings reflect GEPCO's strategic significance as a power utility with exclusive distribution rights within a major agricultural region. The Company's monopoly status and lack of direct competition remain important for ratings.

Strong sponsor profile given GoP ownership

The Company's rating is underpinned by the sponsor support of the GoP. The Company has no long-term or short-term market borrowing and its only long-term borrowing are Relent loans by the GoP. In the past few years, the debt servicing of these Relent loans to the Govt by the company has remained suspended (however accrued in the accounts of the company) under an arrangement with the Govt of receivable/payable settlement. Debt servicing on Relent loans is expected to commence from FY25. The Company has sufficient liquidity in terms of short-term investments and cash in hand in FY24 to liquidate the entire accrued debt service liability. The period of repayment of this liability is to be determined by the GoP. A longer than one-year period would provide further support to the Company.

Profitability is mainly impacted by lag in tariff adjustments.

The Company's revenue is derived from customer contracts and subsidies from the Government of Pakistan (GoP). In FY24, net sales increased by 13.1% to PKR 345.0 bln (FY23: PKR 305.0 bln, FY22: PKR 234.6 bln), primarily driven by a 13.2% increase in customer proceeds due to higher electricity rates and reduced distribution losses, alongside an 11.6% increase in tariff differential subsidies. Despite the revenue growth, gross profit declined to PKR 31.2 bln (FY23: PKR 46.4 bln, FY22: PKR 6.4 bln), resulting in a normalized gross margin of 9.0% (FY23: 15.2%, FY22: 2.7%). The decrease in gross profit is mainly attributed to the lag in monthly fuel cost adjustments (FCA) and higher average purchasing costs from CPPA. Consequently, net profit also fell to PKR 2.3 bln (FY23: PKR 22.9 bln, FY22: PKR -20.3 bln) in FY24, with a reduced net profit margin of 0.7% (FY23: 7.5%, FY22: -8.7%).

The profitability outlook is expected to stabilize with the normalization of timely tariff adjustments. However, potential delays in tariff adjustments may adversely impact profitability in the near term.

Sound coverage and liquidity profile.

In FY24, the Company experienced a decline in its debt service coverage ratio (DSCR), which fell to 1.7x (FY23: 3.5x, FY22: -1.4x). This deterioration in the DSCR can be attributed to a decrease in funds flow from operations (FFO), which amounted to PKR 13.9 bln (FY23: PKR 28.7 bln, FY22: PKR -10.4 bln) in FY24. The decrease in FFO is linked to lower profitability booked during the year on account of delays in customer tariff adjustments during the fiscal year which were booked in the subsequent period.

Meanwhile, the Company has historically maintained a sound liquidity profile with an average 4-year current ratio of 1.7x between FY21-24. The current ratio of reported at 1.4x in FY24 (FY23:

1.70x, FY22: 1.51x). The Company maintains sizeable liquidity on its books by way of short-term investments and cash balances.

Improvement in Capitalization metrics

In FY24, the Company reported an improvement in its capitalization profile, with its gearing ratio improving to 3.70x (FY23: 6.42x, FY22: -0.92x). Similarly, the leverage ratio improved to 41.54x (FY23: 74.72x, FY22: -10.82x). This positive shift in capitalization metrics was primarily driven by an increase in the equity base. The leverage ratio of the Company reflects the policy of the company where substantial deferred tax assets of PKR 63.3 bln in FY23 available to the company are not recognized. Also, the deferred liabilities which largely relate to employee retirement benefits and are payable over a long period of time and which are being funded since FY22 along with customer advances for work are pushing the leverage indicator with gearing remaining in manageable limits except for past years where tariff determination delays impacted gearing.

Gujranwala Electric Power Company Limited — Appendix I

REGULATORY DISCLOSURES

Name of Rated Entity	Gujranwala Electric Power Company Limited
Sector	Power
Type of Relationship	Solicited
Purpose of Rating	Entity Rating
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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Rating History

Rating Date	Medium to Long Term	Short Term	Rating Outlook/Rating Watch	Rating Action
RATING TYPE: ENTITY				
07-Nov-24	AA-	A1	Stable	Initial

Due Diligence Meetings Conducted

S.No.	Name	Designation	Date
1.	Mr. Iyaz Ahmed	Chief Financial Officer (CFO)	September 02nd, 2024
2.	Mr. Irfan Rafique	Director General - MIRAD	