



## RATINGS (JANUARY 2012)

### KOHINOOR ENERGY LIMITED (KEL)

INITIAL

#### ENTITY

Long-term	AA
Short-term	A1+

#### FINANCIAL DATA

(PKR mln)

	Sept 2011	Jun 2011	Jun 2010
Debt-ST	1,682	1,630	200
Equity	7,184	7,258	7,052
Debt-Equity	19:81	19:81	3:97
Efficiency	43%	43%	43%

#### ANALYSTS

Awais Z. Khan  
+92 42 35869504  
awais@pacra.com

Rana Muhammad Nadeem  
+92 42 35869504  
nadeem@pacra.com

#### PROFILE

- Kohinoor Energy Limited (KEL), commencing operations in June 1997, listed on all three local stock exchanges. The main sponsor of the company is Toyota Tsusho Coporation (36%), while Saigol Group (26%), International Finance Corporation (15%), and Wartsila (2%) are other partners. The remaining shareholding is widely dispersed.
- KEL's board comprises seven individuals including the Chief Executive Officer of the company. The board includes four representatives of the TTC (including CEO), two representatives of the Saigol Group (including COO) and one representative of Wartsila Pakistan. Mr. M. Naseem Saigol, chairman of the Saigol Group and a renowned business man, acts as the chairman of the board. The board meets with relatively high frequency and provides active strategic guidance to the top management.

## RATING RATIONALE AND KEY RATING DRIVERS

- The ratings reflect strong financial profile of KEL emanating from low leveraged capital structure – project debt paid off – and guaranteed cash flows by GoP under the Power Purchase Agreement (PPA), subject to adherence to predefined parameters. At the same time, the ratings recognize successful management of Operations and Maintenance (O&M) activities in-house, an outcome of technically sound team, robust systems and controls, and strong governance structure. Only major maintenance tasks are outsourced to Wartsila. Nevertheless, the weak financial discipline of the sole customer, Water and Power Development Authority (WAPDA), is a key consideration.
- In-house management of operations and maintenance function, thereby terminating related risk on the company, has aggravated the importance of the management's ability to perform as per PPA agreed performance parameters. Meanwhile, managing liquidity requirements in the midst of circular debt crisis and external factors such as any changes in the regulatory framework of IPPs remain critical to the ratings.

#### ASSESSMENT

- The total available capacity of electricity generation in Pakistan stands around 21,000MW. However, consistent growths in population, electrification along with industrialization have increased the demand of electricity. In the absence of any noteworthy development in hydel, the government's reliance on thermal generation has increased – particularly IPPs. Therefore, the government incentivized the private sector to setup IPPs. As of now, there are 27 IPPs with installed capacity of ~ 7,584MW, thus, IPPs are playing a critical role to manage the shortfall at acceptable level. However, the power sector has been plagued by the circular debt crisis which has resulted in an accumulation of receivables for the IPPs. In order to ensure smooth and uninterrupted running of the plants, IPPs have resorted to enhance their working capital lines due to late payment by the single buyer (WAPDA/ NTDC). Going forward, GoP's failure to resolve circular debt and consistent piling up of receivable could have a negative implication for the IPPs' sector.
- KEL is an IPP operating under the power policy 1994. The plant, located at Raiwind, near Lahore, consists of eight Residual Fuel Oil fired diesel generators having a capacity of 15.68 MW each alongwith a combined heat cycle recovery system providing an additional output of 8MW through a steam turbine. The company commenced its commercial operation in June 1997.
- Wartsila Finland (WFI), a company of international repute, was contracted for the equipment supply and engineering designs. Wartsila Pakistan – a wholly owned subsidiary of WFI – with a proven track record of providing reliable RFO fired diesel engines in Pakistan was engaged as O&M operator. However, after acquiring the requisite know-how of operating the plant efficiently, KEL is now conducting its O&M activities in-house and has only engaged Wartsila for major maintenance (over 8,000 hrs).
- Pakistan State Oil (PSO), the largest oil-marketing company in Pakistan, is the fuel supplier for KEL. The plant store RFO to provide up to 30 days worth of plant consumption at 100% load factor. However, due to liquidity constraints caused by the circular debt, KEL is holding limited fuel inventory.
- KEL's key source of earnings is the generation tariff from the power purchaser, WAPDA. The reference generation tariff comprises a capacity charge component and an energy charge component. The former is based upon dependable capacity and constitutes a minimum tariff guaranteed to the company which covers the fixed O&M costs, insurance charges, working capital funding costs and return on equity. The latter is a function of actual electricity dispatched.
- Ever since, the management took responsibility of conducting in-house O&M, the efficiency and availability of the plant has been maintained on agreed parameters. Moreover, the plant continues to operate more efficiently. Thus, operating at a higher efficiency level than that agreed upon with the power purchaser, KEL is able to increase profitability, thereby increasing return to shareholders. Meanwhile, KEL has been operating at a high dispatch level over last two years (FY11: 81.78%, FY10: 82.81%) owing to the high electricity demand in the country. KEL dispatched 888,287MWH of electricity in FY11 (FY10: 899,545MWH).
- KEL redeemed its project debt in FY09, therefore, it enjoys a low leveraged capital structure which provides it with financial flexibility and increases its risk absorption capacity. The debt to equity ratio stands at 19% as a result of enhanced working capital requirement (FY11: PKR 3,896mln; FY10: PKR 1,926mln). This has increased due to delayed payment by WAPDA, which is reflected in outstanding receivable (FY11: PKR 1,631mln, FY10: PKR 200mln) of the company. In order to finance the working capital needs, KEL while resorting to short-term borrowing maintains a conservative dividend payout policy to built cushion for contingencies.