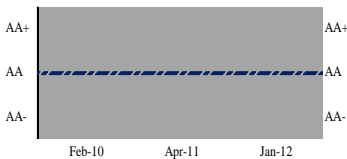


PAK GEN POWER LIMITED (PGPL)

RATINGS (JANUARY 2012)

	NEW	PREVIOUS
ENTITY		
Long Term	AA	AA
Short Term	A1+	A1+

LONG -TERM RATING HISTORY



FINANCIAL DATA

	PKR in mln	
	9MCY11	CY10
Debt-ST	7,265	4,580
Equity	13,053	13,752
Debt /Equity (%)	55.6	33.3
Thermal Efficiency (Avg %)	36.6	36.9
Available Capacity (Avg %)	87.5	94.2
Electricity Generated (GWhrs)	1,420	1,571

ANALYSTS

Naureen Hyat
+92 42 35869504
naureen.hyat@pacra.com

Samiya Mukhtar
+92 42 35869504
samiya@pacra.com

RATING RATIONALE AND KEY DRIVERS

- The ratings reflect strong financial profile of the company as indicated by a sound capital structure and guaranteed cash flows by GoP under the Power Purchase Agreement (PPA), subject to adherence to agreed upon performance benchmarks. PGPL's Operations and Maintenance (O&M) activities are performed in house, exposing the company to sizeable operational risk. However, the O & M team, carrying extensive experience of managing the plant, has been part of the company since long. The team is making efforts to improve the efficiency of the plant, which is currently less than the required level. Meanwhile, the accumulation of circular debt arising from the weak financial discipline of the sole customer, Water and Power Development Authority (WAPDA), is the key challenge faced by the company. Nonetheless, the ratings draw comfort from PGPL's association with the Nishat Group - renowned and financially sound group - which has an explicit commitment to support, in case the need arises.
- The ratings are dependent upon the management's ability to manage and control its operations as per PPA agreed performance parameters. Meanwhile, reaching optimum efficiency, while upholding strong governance and control environment, 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 growth in population and gradual 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. Given its financial constraints, the government incentivized the private sector to setup IPPs. As of now, there are 27 IPPs with installed capacity of ~ 7,500MW. With ~ 36% of the country's total capacity, 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 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 pilling up of receivable could have a negative implication for the IPPs' sector.
- PGPL is an IPP operating under the power policy 1994. The plant, with a capacity of 365 MW, is located at Mehmood Kot, near Muzaffargarh (Punjab) and is based on residual fuel oil (RFO). The plant commenced its commercial production in Feb98. The project has a remaining contractual life of 13 years under PPA with the Power purchaser.
- Nishat Group, the majority shareholder of the PGPL, acquired the company in CY10 from AES Corporation, USA. In July 2011 the company was listed on the Karachi and Lahore stock exchanges and currently has a free float of ~13%. Prior to the acquisition of the company, O&M activities were handled by an in house team trained under the expertise of AES, former O&M operator. This team has been involved in O&M activities since the plant's commencing and hence they carry significant experience. The new sponsors of PGPL have retained the original team thereby largely mitigating any operational risk. However, in house O&M activities have constrained the company's ability to transfer liabilities arising from non-performance onto a third party.
- Pakistan State Oil (PSO), the largest oil-marketing company in Pakistan, is the fuel supplier for PGPL. PSO, under the Fuel Supply Agreement (FSA), delivers RFO to the company through pipelines. The company acquires fuel from PSO on advance payment basis. Moreover, PGPL is required to maintain a fuel inventory of 30 days. However, currently the company is holding less than the required amount of fuel inventory due to cash flow constraints caused by the prevailing circular debt crisis.
- PGPL's key source of revenue is the generation tariff from the power purchaser. It comprises a capacity charge component and an energy charge component. With the exception of agreed return to project shareholders with adjustment for performance achievements, all other elements of cost are pass-through having no bearing on the PGPL's core profitability.
- During 9MCY11, PGPL's average available capacity declined as compared to last year (9MCY11: 87.5%; CY10: 92.3%). However, the company produced more electricity (9MCY11: 1,420GWhr; 9MCY10: 1,323GWhr) on the back of higher demand from WAPDA. The lower production levels in CY10 can be attributed to the onset of flood crisis. During the last few years, the company has been unable to keep its efficiency at the required level of 38% as per the PPA (Average Efficiency Level during 9MCY11: 36.6%; CY10: 36.9%). The management is making efforts to narrow the gap between required and actual efficiency. The company is in the process of installing a 22MW captive power generation plant based on solid waste to meet the demand of auxiliary equipment. This would free up core capacity, improving performance against efficiency benchmark. The plant, with an initial cost of ~PKR 2,000mln, is expected to be installed by CY13.
- Although the company redeemed its project debt in CY10, the debt to equity ratio has increased with rise in short term financing (3QCY11: PKR 7,265mln; CY10: PKR 4,580mln; CY09: PKR 3,000mln). PGPL has lately enhanced its WC lines to PKR 8,750mln (CY09: PKR 5,700mln) in the wake of rising requirements. Nevertheless, the strong equity base of the company and its capacity to absorb risk arising from claim of any Liquidated Damages by WAPDA remains affirm. So far PGPL has utilized 75% of the WC lines. Currently these lines provide the company with sufficient cover against liquidity requirements. The receivables of the company are being financed by WC lines and equity. Although the company has a 90% dividend payout policy, it would be placed better to manage its receivables if it decides to retain most of its profits.

PROFILE

- Pakgen Power Limited (PGPL) is a special purpose company established for electricity generation under the power policy 1994 as an Independent Power Producer (IPP). PGPL, with a total cost of US\$ 347mln, has installed capacity of 365MW. In CY10, the company was acquired by a consortium led by a consortium led by Nishat Group, from AES Corporation, USA. Subsequently, the company was listed on the Karachi and Lahore Stock Exchanges. PGPL redeemed its entire project debt in CY10.
- The principal sponsors of the company are Nishat Group (41%), followed by Abu Dhabi Investment Council (26%) and City Schools (Private) Limited (17%). Majority of board members are nominated by Nishat Group. Mr. Shahid Zulfiqar Khan, the CEO of the company has considerable experience in the power sector. He is also heading the O & M team of the plant.