



The Pakistan Credit Rating Agency Limited

## Rating Report

### Narowal Energy Limited

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#### Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
20-Jun-2024	AA-	A1+	Stable	Maintain	-
22-Jun-2023	AA-	A1+	Stable	Maintain	-
22-Jun-2022	AA-	A1+	Stable	Maintain	-
23-Jun-2021	AA-	A1+	Stable	Maintain	-
25-Jun-2020	AA-	A1+	Stable	Maintain	-
27-Dec-2019	AA-	A1+	Stable	Maintain	-
27-Jun-2019	AA-	A1+	Stable	Maintain	-
27-Dec-2018	AA-	A1+	Stable	Maintain	-
11-Jul-2018	AA-	A1+	Stable	Initial	-

#### Rating Rationale and Key Rating Drivers

The ratings reflect the strong business profile of Narowal Energy Limited (Narowal Energy or the Company) emanating from the demand risk coverage under the Power Purchase Agreement (PPA) signed between CPPA-G and the Company. Meanwhile, the Implementation Agreement provides a sovereign guarantee for cash flows, given adherence to agreed performance benchmarks (Availability: 96%, Efficiency: 45%). The ratings incorporate low operational risk, a result of in-house O&M undertaken by Hub Power Services Limited (HPSL) – an associated company, and adequate insurance coverages. During the period, 9MFY24 Narowal Energy provided ~179GWh (9MFY23 ~321GWh) of electricity to the national grid and recorded sales revenue of PKR ~12,500mln (9MFY22 PKR ~16,224mln), representing a lower demand from the power purchaser. The Company successfully paid off its Long-Term project-related debt in 2021 resulting in a favorable impact on its financial risk profile. As on March 2024, the debt profile majorly comprises short-term borrowings, which have been availed to meet working capital requirements, mainly due to delayed payments from the off-taker. The long-term facility of PKR 2.5bln has also been arranged against which the company is making timely repayments. The announcement of the second interim dividend for FY24 at Rs.7.65 per share echoes the strong equity base of the Company.

The sound financial profile of Hubco; the holding company, provides comfort to the ratings. Adherence to good financial discipline towards both financial and commercial obligations would remain important. Meanwhile, upholding strong operational performance in line with agreed performance levels remains essential.

#### Disclosure

<b>Name of Rated Entity</b>	Narowal Energy Limited
<b>Type of Relationship</b>	Solicited
<b>Purpose of the Rating</b>	Entity Rating
<b>Applicable Criteria</b>	Methodology   Correlation Between Long-term & Short-term Rating Scales(Jul-23),Methodology   Independent Power Producer Rating(Jul-23),Methodology   Rating Modifiers(Apr-24)
<b>Related Research</b>	Sector Study   Power(Jan-24)
<b>Rating Analysts</b>	Andleeb Zahra   andleeb.zahra@pacra.com   +92-42-35869504

## The Pakistan Credit Rating Agency Limited

### Profile

**Plant** Narowal Energy Limited (Narowal Energy) is a 214MW (gross) combined cycle thermal power plant, comprising 11 generating engines from MAN Diesel and one steam turbine from Dresser Rand.

**Tariff** The tariff has been finalized with National Electric Power Regulatory Authority (NEPRA) at the time of Commercial Operations Date in June 2012. The applicable tariff is US 10.77cents/ KWh.

**Return On Project** The ROE is 17% based on NEPRA's approved equity and indexed on quarterly basis as per PPA

### Ownership

**Ownership Structure** Narowal Energy Ltd is 99.99% owned subsidiary of The Hub Power Company Limited (HUBCO). Only four shares are held by only four persons and each has one share only.

**Stability** Stability in the IPPs is drawn from the agreements signed between the Company and the Power Purchaser. Moreover, sponsors association with HUBCO is considered strong.

**Business Acumen** Sponsor groups have significant experience in the energy, cement, dairy, real estate, and finance sector.

**Financial Strength** The financial strength of the sponsors is considered strong as the sponsors have well diversified profitable businesses.

### Governance

**Board Structure** Narowal Energy's Board of Directors comprises of six Directors, including the CEO. The members of the Board are also Board Members of HUBCO. Mr. Kamran Kamal, CEO of the Company, is also the chairman of HUBCO who joined on July 01, 2021.

**Members' Profile** HUBCO's strong professional profile assists the management in terms of strategic guidance and implementation of strong control framework.

**Board Effectiveness** The experiences of board will help guiding the management in developing effective operational and financial policies. No Board Committee is formed by the Board.

**Financial Transparency** PWC A. F. Ferguson & Co. is the external auditor of Narowal Energy and the auditor has given an unqualified report on the financial statements for the year ending June 2023.

### Management

**Organizational Structure** Narowal Energy has a lean organizational structure with an efficient management team. The management control of Narowal Energy vests with Mr. Kamran Kamal, the CEO since 1 July 2021.

**Management Team** Mr. Kamran Kamal, the CEO throughout his 23 years in career has been responsible for large capital projects, building organizational capabilities and for overall business delivery in both management, executive, and Board roles.

**Effectiveness** Narowal Energy's management effectiveness plays a significant role in empowering the organization through positive results, which has made the decision making process systematic. No board committee is formed as the company/board's size is small.

**Control Environment** Narowal Energy has in place an efficient MIS reporting system named Avanceon for its operations. The system generates real-time plant production data, enabling efficient monitoring and timely decision-making.

### Operational Risk

**Power Purchase Agreement** Narowal Energy's key source of earnings is the revenue generated through the sale of electricity to the power purchaser, CPPA-G. The Company will receive the capacity payments if it is at the benchmark availability and is ready to provide electricity, even if no purchase order is placed by Power Purchaser.

**Operation And Maintenance** O&M of Narowal Energy has been outsourced to Narowal Energy's associate Hub Power Services Limited (HPSL). Hub Power Service is a 100% owned subsidiary of HUBCO incorporated to manage the O&M of HUBCO's group power plants.

**Resource Risk** Bakri Trading Company is the fuel supplier for Narowal Plant. The agreed credit period is 30 days, but owing to better supplier relationships the Company can avail credit period of more than 60 days if required.

**Insurance Cover** Narowal Energy Limited has adequate insurance coverage for property damage and business interruption. The insured values for damages include property damage partially disturbed amount of US\$ 1.783 million (up to PKR 509.6mln) & business interruption cover.

### Performance Risk

**Industry Dynamics** Owing to newly installed plants, Pakistan's energy mix is shifting towards Solar/Gas/and coal from Furnace Oil and other expensive sources. The total installed generation capacity was recorded at ~45,885MW at end FY23 (FY22: ~43,775MW, FY21: 39,772MW, FY20: ~38,719MW) up ~3% YoY basis, while actual power generation was recorded at 129,592GWh (FY22: 138,029 (153,874GWh in FY22, down by ~10% YoY basis).

**Generation** The Company has dispatched 180GWh of electricity in 9MFY24 as compared to the previous financial years (FY23: 470GWh, FY22: 868GWh). Resultantly, the load factor remained at 12% as against 23% at 9MFY23.

**Performance Benchmark** The plant's availability remained at 98% at 9MFY24 (FY23: 95%; FY22: 96%) remained well above the required level (95% as per PPA). The Company's profitability increased (FY23: PKR 5,294mln; FY22: PKR 4,005, FY21: PKR 5,869mln, FY20: PKR 4,780mln; FY19: PKR 3,649mln).

### Financial Risk

**Financing Structure Analysis** Narowal Energy has fully paid its project debt in July 2021 without any delay in scheduled repayments. The company had also secured a long-term finance facility of PKR 2.55bln (FY22) under the salary refinancing scheme by SBP which was fully paid in FY22. During 3QFY24 there is no long-term borrowing however current maturity stands at PKR 208mln (FY23: PKR 833mln, FY22: PKR 851mln; FY21: PKR 869mln).

**Liquidity Profile** Receivable days increased (3QFY24: 870days, FY23: 304days; FY22: 291days; FY21: 501days). As circular debt continues to be an issue for companies operating in the power sector. Consequently, IPPs have to manage their liquidity requirements from short-term borrowings.

**Working Capital Financing** Continued lag of payments by CPPA-G has led Narowal Energy's receivables to reach at PKR 12,744mln as at 9MFY24 (Jun23: PKR 16,503mln, Jun22: PKR 20,955mln, Jun21: PKR 22,645mln) out of which 35% are overdue by more than 30 days. The delay in payments from CPPA(G) carries mark-up for all the overdue amounts except LPI invoices. The rate of markup is 3-month KIBOR plus 2% per annum for the first 60 days and there after 3-month KIBOR plus 4.5% per annum. Payables to fuel supplier are not overdue.

**Cash Flow Analysis** The availability of cash flows to repay the debt depends on timely conversion of receivables due from CPPA-G. The coverages of the Company slightly decreased during 3QFY24 (FCFO/Finance Cost: 3QFY24: 9.2x, FY23: 12.1x; FY22: 8.8x; FY21: 8.4x) due to lower FCFOs.

**Capitalization** Long-term project loan is fully repaid by the Company in FY21. However, the Company has a low leveraged capital structure (3QFY24: 9.6%, FY23: 17.1%; FY22: 16%; FY21: 25.5%).



Narowal Energy Ltd. Power	Mar-24 9M	Jun-23 12M	Jun-22 12M	Jun-21 12M
<b>A BALANCE SHEET</b>				
1 Non-Current Assets	11,364	12,120	12,396	13,409
2 Investments	-	-	-	-
3 Related Party Exposure	-	-	-	-
4 Current Assets	19,061	25,108	33,610	27,119
a Inventories	1,764	790	2,982	1,192
b Trade Receivables	12,744	16,503	20,955	22,645
5 Total Assets	30,425	37,228	46,006	40,529
6 Current Liabilities	3,063	3,289	6,883	1,830
a Trade Payables	2,955	3,008	6,791	1,657
7 Borrowings	2,627	5,792	6,289	9,870
8 Related Party Exposure	-	-	-	-
9 Non-Current Liabilities	-	-	-	-
10 Net Assets	24,736	28,147	32,834	28,829
11 Shareholders' Equity	24,736	28,147	32,834	28,829
<b>B INCOME STATEMENT</b>				
1 Sales	4,601	22,452	27,389	15,335
a Cost of Good Sold	(3,300)	(17,031)	(22,601)	(8,444)
2 Gross Profit	1,301	5,421	4,788	6,891
a Operating Expenses	(30)	(86)	(75)	(96)
3 Operating Profit	1,271	5,335	4,713	6,795
a Non Operating Income or (Expense)	27	532	(58)	10
4 Profit or (Loss) before Interest and Tax	1,299	5,867	4,654	6,805
a Total Finance Cost	(234)	(567)	(649)	(935)
b Taxation	(1)	(6)	(1)	(1)
6 Net Income Or (Loss)	1,063	5,294	4,005	5,869
<b>C CASH FLOW STATEMENT</b>				
a Free Cash Flows from Operations (FCFO)	2,111	6,883	5,715	7,821
b Net Cash from Operating Activities before Working Capital Changes	1,627	12,975	(1,476)	6,732
c Changes in Working Capital	1,275	3,087	4,592	(3,445)
1 Net Cash provided by Operating Activities	2,902	16,061	3,116	3,287
2 Net Cash (Used in) or Available From Investing Activities	(16)	(723)	(28)	(54)
3 Net Cash (Used in) or Available From Financing Activities	(7,626)	(10,832)	(869)	(1,434)
4 Net Cash generated or (Used) during the period	(4,740)	4,506	2,219	1,799
<b>D RATIO ANALYSIS</b>				
1 Performance				
a Sales Growth (for the period)	-72.7%	-18.0%	78.6%	10.8%
b Gross Profit Margin	28.3%	24.1%	17.5%	44.9%
c Net Profit Margin	23.1%	23.6%	14.6%	38.3%
d Cash Conversion Efficiency (FCFO adjusted for Working Capital/Sales)	73.6%	44.4%	37.6%	28.5%
e Return on Equity [ Net Profit Margin * Asset Turnover * (Total Assets/S	5.2%	16.8%	13.0%	21.3%
2 Working Capital Management				
a Gross Working Capital (Average Days)	946	335	318	520
b Net Working Capital (Average Days)	769	255	262	491
c Current Ratio (Current Assets / Current Liabilities)	6.2	7.6	4.9	14.8
3 Coverages				
a EBITDA / Finance Cost	9.2	12.1	8.8	8.4
b FCFO / Finance Cost+CMLTB+Excess STB	5.4	4.9	3.8	4.3
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)	0.1	0.1	0.3	0.4
4 Capital Structure				
a Total Borrowings / (Total Borrowings+Shareholders' Equity)	9.6%	17.1%	16.1%	25.5%
b Interest or Markup Payable (Days)	125.8	181.3	51.3	67.3
c Entity Average Borrowing Rate	7.0%	9.0%	7.4%	8.5%
#	Notes			

### Credit Rating

Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

Scale	Long-term Rating Definition
AAA	<b>Highest credit quality.</b> Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments
AA+	
AA	<b>Very high credit quality.</b> Very low expectation of credit risk. Indicate very strong capacity for timely payment of financial commitments. This capacity is not significantly vulnerable to foreseeable events.
AA-	
A+	
A	<b>High credit quality.</b> Low expectation of credit risk. The capacity for timely payment of financial commitments is considered strong. This capacity may, nevertheless, be vulnerable to changes in circumstances or in economic conditions.
A-	
BBB+	
BBB	<b>Good credit quality.</b> Currently a low expectation of credit risk. The capacity for timely payment of financial commitments is considered adequate, but adverse changes in circumstances and in economic conditions are more likely to impair this capacity.
BBB-	
BB+	
BB	<b>Moderate risk.</b> Possibility of credit risk developing. There is a possibility of credit risk developing, particularly as a result of adverse economic or business changes over time; however, business or financial alternatives may be available to allow financial commitments to be met.
BB-	
B+	
B	<b>High credit risk.</b> A limited margin of safety remains against credit risk. Financial commitments are currently being met; however, capacity for continued payment is contingent upon a sustained, favorable business and economic environment.
B-	
CCC	
CC	<b>Very high credit risk.</b> Substantial credit risk "CCC" Default is a real possibility. Capacity for meeting financial commitments is solely reliant upon sustained, favorable business or economic developments. "CC" Rating indicates that default of some kind appears probable. "C" Ratings signal imminent default.
C	
D	Obligations are currently in default.

Scale	Short-term Rating Definition
A1+	The highest capacity for timely repayment.
A1	A strong capacity for timely repayment.
A2	A satisfactory capacity for timely repayment. This may be susceptible to adverse changes in business, economic, or financial conditions.
A3	An adequate capacity for timely repayment. Such capacity is susceptible to adverse changes in business, economic, or financial conditions.
A4	The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions. Liquidity may not be sufficient.



\*The correlation shown is indicative and, in certain cases, may not hold.

**Outlook (Stable, Positive, Negative, Developing)** Indicates the potential and direction of a rating over the intermediate term in response to trends in economic and/or fundamental business/financial conditions. It is not necessarily a precursor to a rating change. 'Stable' outlook means a rating is not likely to change. 'Positive' means it may be raised. 'Negative' means it may be lowered. Where the trends have conflicting elements, the outlook may be described as 'Developing'.

**Rating Watch** Alerts to the possibility of a rating change subsequent to, or, in anticipation of some material identifiable event with indeterminable rating implications. But it does not mean that a rating change is inevitable. A watch should be resolved within foreseeable future, but may continue if underlying circumstances are not settled. Rating watch may accompany rating outlook of the respective opinion.

**Suspension** It is not possible to update an opinion due to lack of requisite information. Opinion should be resumed in foreseeable future. However, if this does not happen within six (6) months, the rating should be considered withdrawn.

**Withdrawn** A rating is withdrawn on a) termination of rating mandate, b) the debt instrument is redeemed, c) the rating remains suspended for six months, d) the entity/issuer defaults, or/and e) PACRA finds it impractical to surveil the opinion due to lack of requisite information.

**Harmonization** A change in rating due to revision in applicable methodology or underlying scale.

**Surveillance.** Surveillance on a publicly disseminated rating opinion is carried out on an ongoing basis till it is formally suspended or withdrawn. A comprehensive surveillance of rating opinion is carried out at least once every six months. However, a rating opinion may be reviewed in the intervening period if it is necessitated by any material happening.

**Note.** This scale is applicable to the following methodology(s):

- a) Broker Entity Rating
- b) Corporate Rating
- c) Debt Instrument Rating
- d) Financial Institution Rating
- e) Holding Company Rating
- f) Independent Power Producer Rating
- g) Microfinance Institution Rating
- h) Non-Banking Finance Companies Rating

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(1) Rating is just an opinion about the creditworthiness of the entity and does not constitute recommendation to buy, hold or sell any security of the entity rated or to buy, hold or sell the security rated, as the case may be | Chapter III; 14-3-(x)

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- i. The Rating Team or any of their family members have no interest in this rating | Chapter III; 12-2-(j)
- ii. PACRA, the analysts involved in the rating process and members of its rating committee, and their family members, do not have any conflict of interest relating to the rating done by them | Chapter III; 12-2-(e) & (k)
- iii. The analyst is not a substantial shareholder of the customer being rated by PACRA [Annexure F; d-(ii)] Explanation: for the purpose of above clause, the term "family members" shall include only those family members who are dependent on the analyst and members of the rating committee

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- (6) PACRA fulfills its obligations in a fair, efficient, transparent and ethical manner and renders high standards of services in performing its functions and obligations; | Chapter III; 11-A-(a)
- (7) PACRA uses due care in preparation of this Rating Report. Our information has been obtained from sources we consider to be reliable but its accuracy or completeness is not guaranteed. PACRA does not, in every instance, independently verifies or validates information received in the rating process or in preparing this Rating Report | Clause 11-(A)(p).
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- (12) PACRA receives compensation from the entity being rated or any third party for the rating services it offers. The receipt of this compensation has no influence on PACRA's opinions or other analytical processes. In all instances, PACRA is committed to preserving the objectivity, integrity and independence of its ratings. Our relationship is governed by two distinct mandates i) rating mandate - signed with the entity being rated or issuer of the debt instrument, and fee mandate - signed with the payer, which can be different from the entity
- (13) PACRA does not provide consultancy/advisory services or other services to any of its customers or to any of its customers' associated companies and associated undertakings that is being rated or has been rated by it during the preceding three years unless it has adequate mechanism in place ensuring that provision of such services does not lead to a conflict of interest situation with its rating activities; | Chapter III; 12-2-(d)
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- (19) PACRA reviews all the outstanding ratings periodically, on annual basis; Provided that public dissemination of annual review and, in an instance of change in rating will be made; | Chapter III | 17-(b)
- (20) PACRA initiates immediate review of the outstanding rating upon becoming aware of any information that may reasonably be expected to result in downgrading of the rating; | Chapter III | 17-(c)
- (21) PACRA engages with the issuer and the debt securities trustee, to remain updated on all information pertaining to the rating of the entity/instrument; | Chapter III | 17-(d)

### **Probability of Default**

(22) PACRA's Rating Scale reflects the expectation of credit risk. The highest rating has the lowest relative likelihood of default (i.e., probability). PACRA's transition studies capture the historical performance behavior of a specific rating notch. Transition behavior of the assigned rating can be obtained from PACRA's Transition Study available at our website. (www.pacra.com). However, actual transition of rating may not follow the pattern observed in the past; | Chapter III | 14-3(f)(vii)

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