



The Pakistan Credit Rating Agency Limited

Rating Report

Sindh Engro Coal Mining Company

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Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
19-Jul-2023	AA	A1+	Stable	Maintain	-
19-Jul-2022	AA	A1+	Stable	Maintain	-
19-Jul-2021	AA	A1+	Stable	Maintain	-
24-Jul-2020	AA	A1+	Stable	Maintain	-
25-Jul-2019	AA	A1+	Stable	Initial	-

Rating Rationale and Key Rating Drivers

Ratings reflect Sindh Engro Coal Mining Company's (SECMC/the Company) ownership structure comprising of the Government of Sindh and financially sound business groups of the Country. In addition to ownership, Ratings also incorporates strategic importance of the project for sustainable energy solution of the Country. SECMC has leased Block-II (out of 12 blocks) of Thar, for the period of thirty (30) years, which has a cumulative capacity of ~1.57bln tonnes of coal which could be used to produce 5,000 MW for fifty (50) years. The Policy for Coal Tariff Determination offers a guaranteed internal rate of return, cost indexation and pass-through tariff structure for SECMC. Comfort is drawn from China Machinery Engineering Corporation (CMEC) – the O&M operator – having significant experience of International EPC projects in Power Plants. Business risk is considered low, exhibited by demand risk coverage as SECMC has signed a Coal Supply Agreements with companies, Engro Powergen Thar Limited (EPTL) for annual supply of 3.8 million tonnes of coal for Phase-I and with Thal Nova Power Thar (Private) Limited (TNPTL) and Thar Energy Limited (TEL) for annual supply of 1.9 million tonnes of coal to each for Phase II and with Lucky Electric Power for annual supply of 3.8 million tonnes of coal for Phase-III. After successful commissioning of Phase-I on 10th July 2019, the COD of Phase-II is achieved on September 30, 2022. Project Completion date (PCD) for Phase-I has been announced in May 2023. Phase-III is in pipeline and its financial close is expected in 4QCY23. SECMC has reported its topline of PKR 21.8bln during 1QCY23. The Company incurred net loss of PKR 3.7bln due to massive exchange loss of PKR 8.6bln. Since \$ based indexation is allowed in tariff, this item is recoverable in due course. Strong liquidity and performance has enabled timely repayment of all the due loan repayments. While going forward, with the draw down for phase-III, leveraging is expected to rise. Though short-term borrowing has enhanced as compared to SPLY but strong cash position depicts good financial health of the Company.

Adherence to good financial discipline towards both financial and commercial obligations is considered a strength. Meanwhile, upholding strong operational performance in line with agreed performance levels remain important. Effective management of the project, favorable regulatory regime, and consistency in related policies remain critical for the ratings. The ratings incorporate the prevailing challenges on account of circular debt crisis. Company's liquidity situation in terms of pending receivables seems stringent.

Disclosure

Name of Rated Entity	Sindh Engro Coal Mining Company
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology Corporate Rating(Jun-22),Methodology Correlation Between Long-term & Short-term Rating Scales(Jun-22),Methodology Rating Modifiers(Jun-22)
Related Research	Sector Study Coal Mining and Trading(Jul-22)
Rating Analysts	Anam Waqas Ghayour anam.waqas@pacra.com +92-42-35869504



Coal Mining and Trading

The Pakistan Credit Rating Agency Limited

Profile

Legal Structure Sindh Engro Coal Mining Company Limited is a public unlisted company, incorporated in Pakistan on October 15, 2009. The Company has its registered office at, The Harbor Front Building, Clifton, Karachi

Background The Company had commenced an initial feasibility study of the project in November 2009 through a team of International Consultants and local experts to confirm the technical, environmental, social and economic viability of the Project. The study was carried out on an area of 79.6 sq. km allocated to the Company in Thar Coalfield which was approved by the Technical Committee of the Government of Sindh on August 31, 2010.

Operations The Company was formed under a Joint Venture Agreement, dated September 8, 2009, between the Government of Sindh (GoS), Engro Energy Limited (EEL) [formerly Engro Powergen Limited (EPL)] and Engro Corporation Limited for the development, construction and operations of an open-cast lignite mine in Block II of Thar Coal Field, Sindh.

Ownership

Ownership Structure The company's ordinary shares, ~91.5% of the total equity, are owned by Government of Sindh (~54.70%), Engro Energy Limited (~11.90%), Thal Limited (~11.90%), Habib ank Limited (~9.50%), HUBCO (~8%), and CMEC Thar Mining Investments LTD (~4%). While preference shares, ~8.5% of the total equity, are owned by Huolinhe Open Pit Coal (HK) Investment Co. Ltd (100%).

Stability Majority shareholding owned by Government of Sindh provides support to stability of the company. Comfort is also drawn as the country's biggest conglomerate, Engro Corporation Limited (ECorp), has its stake in the company through its subsidiary company, Engro Energy Limited, and Mega Conglomerate Private Limited through its subsidiary company HUBCO.

Business Acumen Government of Sindh holds SECMC as its strategically vital asset, whereas more technical knowledge flows in from Engro, HUBCO & CMEC. The business acumen of sponsors of the company is considered strong.

Financial Strength Joint ownership from the Government of Sindh (GoS) and association of financially sound conglomerates provide absolute financial strength to the company. Given the strategic importance of SECMC to the GoS, in terms of its socio-economic policies and its quest of reducing the import bill, the probability of sovereign support, in case the company requires it, remains high.

Governance

Board Structure The board of SECMC comprises twelve experienced professionals, five members represents Government of Sindh, two nominees are from Engro, two members appertaining to Thal Limited, while Habib Bank Limited, HUBCO and Huolinhe Investment company represent one member each.

Members' Profile Imtiaz Ahmed Sheikh is the Chairman of the board. He is a seasoned Pakistani politician who is the current and Provincial Minister of Sindh for Energy, in office since 5 September 2018. He has been a member of the Provincial Assembly of Sindh since August 2018.

Board Effectiveness During FY22, the board held nine meetings to address the strategic decisions of the company. There are five committees at the Board level, namely i) Audit Committee, ii) Risk Management committee, iii) Peoples Committee, iv) Procurement Committee, v) CSA Committee

Financial Transparency A. F. Ferguson & Co., a member firm of PWC, is the auditor of the company. They expressed an unqualified opinion on the company's financial statements at end-Dec'22. Though the company is non-listed, still financial statements have been being prepared in a timely fashion to maintain financial transparency intact.

Management

Organizational Structure Company's organization is structured around the effective functioning of seven major departments. Each department is headed by an experienced professional, reporting directly to the CEO. The departments comprise: a) Finance, b) HR & Admin, c) Site Operations, d) Mine Tech & Expansion, e) Water Resources, f) Commercial Operations, & g) Audit.

Management Team Mr. Amir Iqbal is the Chief Executive Officer of the Company. He has over 27 years of experience in general management and has led various teams in sales and marketing function across Pakistan, Australia, and Africa. He has managed various global and local mega brands and led cross functional teams to deliver business results.

Effectiveness To oversee the management of the company, SECMC has constituted an internal management committee comprising of executives from SECMC and of all subsidiaries Engro Energy Limited. The purpose of the committee is to drive the strategic decision making for the company and formulates new strategies to deal with developments that the company encounters.

MIS SECMC uses SAP as its Enterprise Resources Planning (ERP) Software specifically the FICO (Finance Module) for maintaining its financial database. SAP FI is made up of submodules. The sub-modules that are often used to generate reports of accounts receivables, accounts payables, asset accounting, general ledger accounting and bank accounting.

Control Environment SECMC maintains an effective control environment with defined policies and procedures. Company's internal audit function performs regular reviews on the financial, operational and compliance controls and reports directly to the audit committee for all critical issues.

Business Risk

Industry Dynamics Pakistan's total coal reserves stood at ~185,175mtn tonnes and is ranked seventh amongst the lignite (coal) rich countries of the world. Of all the reserves ~99% of the reserves are present in Sindh province, while Punjab, and Baluchistan shares ~0.1% each to the total reserves. The country's largest coal reserves are located at Tharparkar District in the south-eastern province of Sindh, where about ~175,506mtn Tonnes is identified, which is ~94% of the total reserves and ~95% of the reserves in Sindh Province

Relative Position SECMC project is being developed in Block II. It has total reserves of ~1,584mtn tonnes which is ~1% of the total reserves in Thar region of Sindh. It is estimated that exploitable reserves of 1,584mtn tons can be used to produce 5,000 MW for fifty years.

Revenues Company's revenue source is a component of i) Tariff that is being charged to its customer, and ii) coal that will be supplied. First year tariff for phase-I determined at the time of COD is \$61.64 per ton. Company has started operations in July-19 and at 3MCY23 company's revenue generation is reported at PKR 21,759mtn (CY22: PKR 51,598mtn).

Margins During 3MCY23, Company's gross margin has been reported at 34.1% in comparison to 53.1% during 3MCY22. Company has posted a net loss of PKR 3,785mtn at end Mar'23 (3MCY22: PKR 3,127mtn) on account of trickledown effect of exchange currency loss and increased finance cost. Hence, company's net margin has turned negative to 17.4% (3MCY22: 32.3%).

Sustainability Coal is mostly imported in Pakistan to meet domestic demand and, although imported coal is a cheap source of fuel compared to imported oil. With the development of Pakistan's huge coal reserves at Thar, the country will be able to substitute its use of imported oil and, through the use of affordable and sustainable energy sources

Financial Risk

Working Capital During 3MCY23 company's net working capital cycle stood at 228days compared 304days in 3MCY22. SECMC manages its working capital cycle through mix of internal cashflows and short term borrowings. During review, Company's reliance on short term borrowings stands PKR 8,640mtn.

Coverages As per 3MCY23, FCFO of the Company stood at PKR 4,340mtn (3MCY22: PKR 6,612mtn). In the midst of this deterioration in 3MCY23, coverages were also impacted heavily [Interest Coverage: 3MCY23: 1.6x, 3MCY22: 5.4x, CY22: ~3.4x].

Capitalization The total project cost of phase I was ~USD 626.8mtn which is being financed with a debt to equity ratio of 75:25. Debt portion is a mix of local and foreign financing. The first principal payment for the same was due in June-20 and the respective obligation is timely fulfilled by the entity. Phase II has a total project cost of USD 173mtn. The debt portion comprises of local financing of USD 149mtn respectively.



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Sindh Engro Coal Mining Company Coal Mining and Trading	Mar-23 3M	Dec-22 12M	Dec-21 12M	Dec-20 12M
A BALANCE SHEET				
1 Non-Current Assets	96,179	97,007	87,033	77,376
2 Investments	-	-	-	-
3 Related Party Exposure	206	206	206	206
4 Current Assets	133,268	105,009	71,528	46,526
a Inventories	2,530	994	683	667
b Trade Receivables	58,636	46,616	31,785	26,178
5 Total Assets	229,653	202,222	158,767	124,107
6 Current Liabilities	73,820	59,028	37,551	20,754
a Trade Payables	-	-	-	-
7 Borrowings	99,288	84,111	70,027	67,402
8 Related Party Exposure	-	-	-	-
9 Non-Current Liabilities	-	-	-	-
10 Net Assets	56,545	59,083	51,190	35,951
11 Shareholders' Equity	56,545	59,083	51,190	36,205
B INCOME STATEMENT				
1 Sales	21,759	51,598	39,111	37,101
a Cost of Good Sold	(14,331)	(31,947)	(21,336)	(19,470)
2 Gross Profit	7,429	19,651	17,775	17,631
a Operating Expenses	(452)	(808)	(699)	(656)
3 Operating Profit	6,976	18,843	17,076	16,975
a Non Operating Income or (Expense)	(6,761)	(2,174)	(1,486)	(299)
4 Profit or (Loss) before Interest and Tax	215	16,670	15,590	16,676
a Total Finance Cost	(3,411)	(7,202)	(4,177)	(6,717)
b Taxation	(589)	(1,574)	(405)	14
6 Net Income Or (Loss)	(3,785)	7,894	11,008	9,972
C CASH FLOW STATEMENT				
a Free Cash Flows from Operations (FCFO)	4,340	24,446	21,525	19,520
b Net Cash from Operating Activities before Working Capital Changes	7,628	17,321	16,813	12,960
c Changes in Working Capital	(3,408)	4,846	9,549	1,727
1 Net Cash provided by Operating Activities	4,220	22,168	26,363	14,687
2 Net Cash (Used in) or Available From Investing Activities	(688)	(12,700)	(12,333)	(8,641)
3 Net Cash (Used in) or Available From Financing Activities	7,640	6,437	3,491	838
4 Net Cash generated or (Used) during the period	11,172	15,904	17,521	6,884
D RATIO ANALYSIS				
1 Performance				
a Gross Profit Margin	34.1%	38.1%	45.4%	47.5%
b Net Profit Margin	-17.4%	15.3%	28.1%	26.9%
c Cash Conversion Efficiency (FCFO adjusted for Working Capital/Sales)	4.3%	56.8%	79.5%	57.3%
d Return on Equity [Net Profit Margin * Asset Turnover * (Total Assets/Sh	-9.1%	27.8%	46.3%	55.1%
2 Working Capital Management				
a Gross Working Capital (Average Days)	609	147	145	132
b Net Working Capital (Average Days)	609	147	145	132
c Current Ratio (Current Assets / Current Liabilities)	1.8	1.8	1.9	2.2
3 Coverages				
a EBITDA / Finance Cost	1.6	3.4	5.4	2.9
b FCFO / Finance Cost+CMLTB+Excess STB	0.4	2.4	3.4	2.2
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)	64.5	2.3	1.9	2.5
4 Capital Structure				
a Total Borrowings / (Total Borrowings+Shareholders' Equity)	63.7%	58.7%	57.8%	65.1%
b Interest or Markup Payable (Days)	360.2	28.1	22.8	10.3
c Entity Average Borrowing Rate	5.3%	17.6%	11.4%	20.0%

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	Highest credit quality. Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments
AA+	
AA	Very high credit quality. 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	High credit quality. 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+	Good credit quality. 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	
BBB-	
BB+	Moderate risk. 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	
BB-	
B+	
B	High credit risk. 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	Very high credit risk. 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.
CC	
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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Rating Team Statements

(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)

2) Conflict of Interest

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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(4) PACRA does not disclose or discuss with outside parties or make improper use of the non-public information which has come to its knowledge during business relationship with the customer | Chapter III; 10-7-(d)

(5) PACRA does not make proposals or recommendations regarding the activities of rated entities that could impact a credit rating of entity subject to rating | Chapter III; 10-7-(k)

Conduct of Business

(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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(9) PACRA ensures before commencement of the rating process that an analyst or employee has not had a recent employment or other significant business or personal relationship with the rated entity that may cause or may be perceived as causing a conflict of interest; | Chapter III; 11-A-(r)

(10) PACRA maintains principal of integrity in seeking rating business | Chapter III; 11-A-(u)

(11) PACRA promptly investigates, in the event of a misconduct or a breach of the policies, procedures and controls, and takes appropriate steps to rectify any weaknesses to prevent any recurrence along with suitable punitive action against the responsible employee(s) | Chapter III; 11-B-(m)

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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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(15) PACRA ensures that the rating assigned to an entity or instrument is not be affected by the existence of a business relationship between PACRA and the entity or any other party, or the non-existence of such a relationship | Chapter III; 12-2-(i)

(16) PACRA ensures that the analysts or any of their family members shall not buy or sell or engage in any transaction in any security which falls in the analyst's area of primary analytical responsibility. This clause shall, however, not be applicable on investment in securities through collective investment schemes. | Chapter III; 12-2-(l)

(17) PACRA has established policies and procedure governing investments and trading in securities by its employees and for monitoring the same to prevent insider trading, market manipulation or any other market abuse | Chapter III; 11-B-(g)

Monitoring and review

(18) PACRA monitors all the outstanding ratings continuously and any potential change therein due to any event associated with the issuer, the security arrangement, the industry etc., is disseminated to the market, immediately and in effective manner, after appropriate consultation with the entity/issuer; | Chapter III | 18-(a)

(19) PACRA reviews all the outstanding ratings on semi-annual basis or as and when required by any creditor or upon the occurrence of such an event which requires to do so; | Chapter III | 18-(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 | 18-(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 | 18-(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-(F-VII)

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