The Pakistan Credit Rating Agency Limited

Rating Report

Thar Energy Limited

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
25-Oct-2024	AA-	A1	Stable	Maintain	-
25-Oct-2023	AA-	A1	Stable	Upgrade	-
16-Feb-2023	A	A2	Stable	Upgrade	-
12-Sep-2022	A-	A2	Stable	Maintain	Yes
23-Sep-2021	A-	A2	Stable	Maintain	Yes
24-Sep-2020	A-	A2	Stable	Initial	Yes

Rating Rationale and Key Rating Drivers

The Hub Power Company Limited (HUBCO) of Pakistan, along with Fauji Fertilizer Company Limited (FFCL) and China Machinery Engineering Corporation (CMEC) TEL Investment, has set up a 330 MW mine-mouth lignite-fired power plant at Thar Coal Block-II Sindh, under the umbrella of Thar Energy Limited (TEL). The plant is part of the China Pakistan Economic Corridor (CPEC) and is fueled by coal extracted from Thar Block-II by the Sindh Engro Coal Mining Company. Being on local coal, the plant reduces dependence on imported fuels and resultantly positively affects the overall basket price of the electricity generated. The plant is prioritized in the merit order list by NTDC due to its low generation cost. Additionally, the plant efficiency and utilization factor are high. TEL has been awarded an upfront tariff, with the payments to be received from CPPA-G against energy and capacity, backed by a sovereign guarantee. The plant successfully achieved its Commercial Operations (COD) on October 1, 2022. As per the Power Purchase Agreement (PPA), CPPA-G has charged Liquidated Damages amounting to USD 7.70mln due to delay in achievement of COD beyond Required Commercial Operations Date (RCOD) for the period 23rd November 2021 to 30th September 2022. In accordance with the agreement, Hub Power Services Limited (HPSL), an associated company, will provide operations and maintenance (O&M) services for the plant. The O&M contractor will be responsible for maintaining the operational benchmarks (availability: 85%, efficiency: 37%). During FY24, the net electrical output of the plant stood at 1,940 GWh (FY23: 1,053 GWh) with a load factor of 73.4% while maintaining its operational benchmarks. Currently, the working capital requirements are managed through a mix of internal cash generation and short-term borrowings from banks. Going forward, future borrowings are dependent on the rising operational needs along with the repayment behavior of the power purchaser against outstanding receivables.

Timely repayment of project debt along with successfully meeting operational benchmarks remains crucial to upholding the assigned ratings. Furthermore, considering the ongoing developments in the power sector, any modification in the long-term agreements might potentially impact the ratings.

Disclosure

Name of Rated Entity	Thar Energy Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology | Rating Modifiers(Apr-24),Methodology | Correlation Between Long-term & Short-term Rating Scales(Jul-24),Methodology | Independent Power Producer Rating(Jul-24)
Related Research	Sector Study | Power(Jan-24)
Rating Analysts	Hashim Yazdani | hashim.yazdani@pacra.com | +92-42-35869504

Profile

Plant Thar Energy Limited (TEL) is an independent power producer (IPP) and has developed a 330 MW coal-fired power plant in Thar Block II on a build-own-Operate (BOO) basis. The plant achieved its commercial operations date (COD) on October 1, 2022.

Tariff TEL is awarded an upfront tariff for coal power projects by NEPRA of US¢8.5015/KWh. Tariff control period is 30 years from the COD. The tariff is indexed to the Pakistan rupee-US dollar exchange rate and US and Pakistan CPI inflation. Principal and interest repayments, ROE, insurance, fixed and variable O&M costs are part of the scalable (adjustable) component. Fuel price and all the taxes/levies are completely passed through to the power purchaser.

Return On Project As per the agreement with NEPRA, the return on equity (ROE) of the project is 30.65%, which is a component of the tariff allocated to TEL.

Ownership

Ownership Structure TEL’s main sponsors are The Hub Power Company Limited (HUBCO), Fauji Fertilizer Company Limited, and China Machinery and Engineering Corporation (CMEC) TEL . HUBCO Group has the controlling interest of 60%, Fauji Fertilizer at 30%, and CMEC TEL Investments has 10% ownership.

Stability Stability in the ownership is derived from long-term strategic investment in the company by sponsoring groups, including HUBCO and the Fauji Group.

Business Acumen Sponsor groups have a proven history of development and operations of power projects in the country that produce electricity from different sources, including thermal, coal, and renewable. HUBCO, being the major shareholder, is the largest private power producer of the country.

Financial Strength Having business interests in various sectors, both HUBCO and Fauji Group are among the leading conglomerates of the country with strong financial muscle.

Governance

Board Structure TEL's Board of Directors (BoD) comprises eight members, including seven non-executive members along with the CEO. Both HUBCO and Fauji Fertilizer Company Limited have three members each on the board, while one member represents CMEC.

Members’ Profile Mr. Kamran Kamal is the Chairman of the Board of Directors of TEL and also the CEO of The Hub Power Company Limited (HUBCO). He has been associated with HUBCO Group in various capacities and brings vast experience of the local power sector. The remaining members also possess sufficient experience in their respective fields.

Board Effectiveness The board conducts regular meetings to discuss matters relating to the Company's operations and financials, along with providing supervision and granting approval for other policies of the Company.

Financial Transparency The management ensures timely preparation of accounts along with maintenance of financial records relating to invoices to the power purchaser. A. F. Ferguson & Co. Chartered Accountants are the external auditors of the company.

Management

Organizational Structure IPPs are generally featured by a flat organizational structure, mainly comprising finance and treasury staff, while the engineering, construction, and operations of the plant are outsourced to third-party contractors.

Management Team Mr. Amjad Ali Raja has been appointed as the new CEO in July 2024. He has been associated with the HUBCO group since 2013. With an engineering background, Mr. Amjad brings 22 years of experience in the energy sector. The remaining team of individuals possesses prerequisite qualifications and experience to perform the required functions.

Effectiveness The management is majorly engaged in operational matters relating to the Company, including invoicing to CPPAG, internal audit, preparation of accounts, treasury operations, and tariff determination, while the plant's operations and maintenance are outsourced.

Control Environment The management has developed a comprehensive internal audit function that ensures timely delivery of data and reports. Furthermore, the operation and maintenance contractors deliver reports to the management relating to the plant operations to ensure smoothness.

Operational Risk

Power Purchase Agreement The Company has entered into a 30-year Power Purchase Agreement with Central Power Purchasing Agency (CPPA-G) under which it will supply electricity to the power purchaser and generate invoices relating to Energy Purchase Price and Capacity Purchase Price.

Operation And Maintenance TEL has entered into a long-term contract with Hub Power Services Limited (HPSL) to manage the plant's operation and maintenance. HPSL is a subsidiary of the HUBCO Group, which is also engaged in providing O&M services for other plants of the group.

Resource Risk TEL is sourcing coal from Sindh Engro Coal Mining Company (SECMC) under their 30-year Coal Supply Agreement that was signed at the inception of the project.

Insurance Cover Insurance is attained for material damage, third party liability, and delay in startup affecting the profits. Contractors will be liable to pay Liquidated Damages (LDs) as per the contract if the benchmark performance ratio is not met.

Performance Risk

Industry Dynamics Pakistan power generation during FY-2024 fell by 1.9 percent to 127,160 GWh, marking the second consecutive annual decline due to higher electricity costs, rising inflation, and a decrease in economic activity in the country. Hydropower remained the largest source of power generation, accounting for 31% of the total. RLNG-based power generation contributed 19%, while local coal-based power plants contributed 12%. Nuclear power generation share stood at 19%. The remaining was met through other thermal sources, including imported coal, while a minor share was contributed through renewable resources, including wind and solar.

Generation Net electrical output of the plant during FY24 stood at 1,940 GWh (FY23: 1,053 GWh) with a load factor of 73.4%. The power purchaser sources electricity from the plant on priority due to its low cost of generation.

Performance Benchmark The required availability for Thar Energy Limited under the PPA is 85%. Meanwhile, the required efficiency of the plant is 37%. On average, the plant maintained its required benchmarks throughout the period.

Financial Risk

Financing Structure Analysis The actual project cost is USD 520mln, debt financing constitutes 75% (USD 390mln). Total project debt has been funded by a mix of foreign (~67%) and local debt (~33%). The foreign debt has been sponsored by Chinese lenders with the consortium led by CDB and China Minsheng Banking Corporation Limited. Foreign debt has the pricing of 6ML + 4.05% spread p.a. payable semi-annually. The local debt has been sponsored by Pakistani banks with the consortium led by Bank Alfalah Limited, including HBL, BAHL, NBP, MCB, SBL, and Soneri Bank Limited. Local debt has the pricing of 3MK + 3.5% spread p.a. payable semi-annually. Currently, the Company has repaid approximately 10% of the project debt.

Liquidity Profile TEL, in its off-take agreement with CPPA-G, will receive capacity payments given the plant meets contract availability, even if no purchase order is placed. As of June 2024, the Company's trade receivables from CPPAG stood at PKR 15,364mln. 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 and internal cash generation.

Working Capital Financing Due to rising trade receivables from CPPPAG, gross working capital stood at 69 days as of June 2024. The Company is managing its working capital requirements through a mix of internal cash generation and short term lines availed from banks. Future financing depends on the payment behavior of the power purchaser against outstanding receivables.

Cash Flow Analysis During FY24, the Company reported FCFO of PKR 25,602mln from the sale of electricity to CPPAG. EBIDTA/Finance Cost stood at 2.09x. Cash flow position is expected to improve with increased generation in the coming period since the plant is placed on priority in the merit order list.

Capitalization As on June 2024, leveraging stood at 72.0% which is mainly attributable to long term project debt.

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Financial Summary
PKR mln

Thar Energy Limited Power	Jun-24 12M	Jun-23 12M	Jun-22 12M	Jun-21 12M
A BALANCE SHEET				
1 Non-Current Assets	101,665	106,858	73,753	41,303
2 Investments	500	-	-	-
3 Related Party Exposure	28	-	8	8
4 Current Assets	49,535	33,331	3,206	697
a Inventories	*585*	*181*	-	-
b Trade Receivables	*15,364*	*7,317*	-	-
5 Total Assets	151,728	140,189	76,967	42,008
6 Current Liabilities	26,466	19,071	3,035	23,806
a Trade Payables	*15,877*	*11,869*	*702*	*147*
7 Borrowings	88,555	93,223	58,449	3,195
8 Related Party Exposure	2,186	3,095	430	3,247
9 Non-Current Liabilities	-	-	-	-
10 Net Assets	34,520	24,801	15,052	11,761
11 Shareholders' Equity	34,520	24,801	15,052	11,761
B INCOME STATEMENT				
1 Sales	61,875	37,869	-	-
a Cost of Good Sold	*(39,142)*	*(22,969)*	-	-
2 Gross Profit	22,734	14,900	-	-
a Operating Expenses	(220)	(228)	(144)	(36)
3 Operating Profit	22,513	14,672	(144)	(36)
a Non Operating Income or (Expense)	*818*	*(960)*	*105*	*(17)*
4 Profit or (Loss) before Interest and Tax	23,332	13,711	(39)	(53)
a Total Finance Cost	*(13,310)*	*(7,848)*	*(0)*	*(0)*
b Taxation	*(286)*	*(67)*	*(7)*	*(2)*
6 Net Income Or (Loss)	9,736	5,797	(46)	(55)
C CASH FLOW STATEMENT				
a Free Cash Flows from Operations (FCFO)	*25,602*	*15,704*	*(78)*	*(53)*
b Net Cash from Operating Activities before Working Capital Changes	*13,733*	*9,433*	*(4,586)*	*(46)*
c Changes in Working Capital	*1,293*	*(11,757)*	*1,666*	*7,396*
1 Net Cash provided by Operating Activities	15,026	(2,324)	(2,921)	7,350
2 Net Cash (Used in) or Available From Investing Activities	(1,342)	(14,072)	(49,748)	(9,173)
3 Net Cash (Used in) or Available From Financing Activities	(845)	18,158	53,899	1,252
4 Net Cash generated or (Used) during the period	12,839	1,762	1,230	(571)
D RATIO ANALYSIS				
1 Performance				
a Sales Growth (for the period)	63.4%	N/A	N/A	N/A
b Gross Profit Margin	36.7%	39.3%	N/A	N/A
c Net Profit Margin	15.7%	15.3%	N/A	N/A
d Cash Conversion Efficiency (FCFO adjusted for Working Capital/Sales)	43.5%	10.4%	N/A	N/A
*e Return on Equity [Net Profit Margin * Asset Turnover * (Total Assets/Shareholders' Equity)]*	29.3%	30.2%	N/A	N/A
2 Working Capital Management				
a Gross Working Capital (Average Days)	69	72	N/A	N/A
b Net Working Capital (Average Days)	-13	12	N/A	N/A
c Current Ratio (Current Assets / Current Liabilities)	1.9	1.7	1.1	0.0
3 Coverages				
a EBITDA / Finance Cost	2.0	2.2	N/A	N/A
b FCFO / Finance Cost+CMLTB+Excess STB	1.4	1.0	N/A	0.0
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)	6.3	10.8	-744.9	-496.3
4 Capital Structure				
a Total Borrowings / (Total Borrowings+Shareholders' Equity)	72.0%	79.0%	79.5%	21.4%
b Interest or Markup Payable (Days)	152.0	234.0	N/A	N/A
c Entity Average Borrowing Rate	13.7%	10.0%	0.0%	0.0%

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
AAA	Highest credit quality. Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments
AA+ 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.
A+ 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.
BBB+ BBB 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.
BB+ BB 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.
B+ 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.
CCC CC C	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.
D	Obligations are currently in default.

Scale	Short-Term Rating
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.

Rating Modifiers | Rating Actions

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. Rating actions may include "maintain", "upgrade", or "downgrade".

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 Company

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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)

2) **Conflict of Interest**
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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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(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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(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)
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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 | 17-(a)
(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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