



The Pakistan Credit Rating Agency Limited

## Rating Report

### Foundation Power Company Daharki Limited

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#### Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
30-Apr-2019	AA-	A1+	Stable	Maintain	-
22-Nov-2018	AA-	A1+	Stable	Maintain	-
30-Apr-2018	AA-	A1+	Stable	Maintain	-
16-Oct-2017	AA-	A1+	Stable	Upgrade	-
24-Mar-2017	A+	A1	Positive	Maintain	-

#### Rating Rationale and Key Rating Drivers

The ratings reflect strong business profile of Foundation Power Company Daharki Limited (Foundation Power) emanating from the demand risk coverage under Power Purchase Agreement signed between NTDC (through Central Power Purchasing Agency) and the company. Meanwhile, the Implementation Agreement provides sovereign guarantee for cashflows, given adherence to agreed performance benchmarks. The ratings incorporate low operational risk, a result of the performance of KEPCO - the O&M operator. Fuel of the plant is 'low BTU' gas, which is supplied by an associate - Mari Petroleum Company Limited (40% owned by Fauji Foundation). Thus, fuel supply risk is considered low. Although there are delays in payments from power purchaser, the company manages the impact by aligning the payments to fuel supplier with its receipts. This keeps working capital needs under check. Short-term borrowing lines are available and available cushion therein is significant at end-Dec18, which provides comfort. Foundation Power has total long-term debt of PKR 3,794mln as at end-Dec18 payable till June 2020. Moreover, Foundation Power has been repaying its debt repayments (Principal and Markup) on time without availing benefit of forbearance period. The company's association with Fauji Foundation (FF) provides comfort to the ratings.

Sustained good financial discipline and upholding strong operational performance in line with agreed performance levels remain important. Accumulation of circular debt would pose threat to the company's ability to continue with this practice. However, the management ably supported by sponsors remains committed to sustain improvement in management of commercial obligations and timely debt repayments.

#### Disclosure

<b>Name of Rated Entity</b>	Foundation Power Company Daharki Limited
<b>Type of Relationship</b>	Solicited
<b>Purpose of the Rating</b>	Entity Rating
<b>Applicable Criteria</b>	Methodology   Criteria   Rating Modifier(Jun-18),Methodology   Correlation Between Long-Term And Short-Term Rating Scale(Jun-18),Methodology   IPP (Jun-18)
<b>Related Research</b>	Sector Study   Power(Jan-19)
<b>Rating Analysts</b>	Faizan Arif   faizan.sufi@pacra.com   +92-42-35869504

## The Pakistan Credit Rating Agency Limited

### Profile

**Plant** Foundation Power Company Daharki Limited (Foundation Power), a public limited company, is operating a combined cycle power plant on a build-own-operate (BOO) basis with a net initial capacity of 180MW (7.8MW auxiliary consumption)

**Tariff** Foundation Power key source of earnings is the generation tariff from the power purchaser, NTDC. The reference generation tariff comprises a capacity charge component and an energy charge component. Foundation Power's levelized tariff is US¢ 6.55/kWh.

**Return On Project** The dollar IRR of Foundation Power, as agreed with NEPRA, is 15%.

### Ownership

**Ownership Structure** Foundation power is majority owned by Daharki Power Holdings Limited (DPHL), which, in turn is owned by Fauji Foundation (FF) (81%) and Asian Development Bank (ADB) (19%).

**Stability** Stability in the IPPs is drawn from the agreements signed between the company and power purchaser. However, sponsors association with Fauji Foundation group and Asian Development Bank will continue to provide comfort.

**Business Acumen** Sponsor groups have significant experience in the manufacturing and selling of energy, fertilizer, cement and chemicals.

**Financial Strength** Fauji Foundation (also known as Fauji Group), is amongst the largest business conglomerate in Pakistan. The financial strength of the sponsors is considered strong as the sponsors have well diversified profitable businesses.

### Governance

**Board Structure** The six-member Board, comprising five representatives from Fauji Foundation and one from Asian Development Bank (presently awaiting nomination for designate as a replacement to previous nominee director) provides adequate guidance to the company. Newly appointed in 2018, Lt. Gen. Syed Tariq Nadeem Gilani (Retd.) – Managing Director of Fauji Foundation – is the Chairman of the Board.

**Members' Profile** Fauji Foundation'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. The board has formulated three committees, i) Audit and Finance Committee, ii), Technical Committee and (iii) Human Resource Committee to ensure smooth and effective monitoring of operations. Participation of all board members during board meetings remained satisfactory.

**Financial Transparency** A.F. Ferguson & Co. has been engaged as Foundation Power's external auditors. The auditors expressed an unqualified opinion on the audited financial statements of the company for the year ended June 30, 2018.

### Management

**Organizational Structure** Foundation Power has a lean management structure, mainly comprises finance, internal audit and technical staff. The management control of the company vests with Daharki Power Holdings Limited (DPHL), which, in turn is owned by Fauji Foundation (FF), being largest shareholder.

**Management Team** Maj Gen Asghar Nawaz, HI(M) (Retd), Managing Director of Foundation Power Company replaced Lt. Gen. Jamil Haider (Retd) in August 2018. He had a distinguished career in the Pakistan Army. The management team is experienced and is ably handling the affairs of the company.

**Effectiveness** The management of Foundation Power is mostly engaged in the finance related activities. The operations and maintenance of the plant have been outsourced to KEPCO Plant Service & Engineering Company Limited (KEPCO). The management has engaged three site engineers, with the title of managers, who maintain daily correspondence with the O&M team to ensure oversight and liaison with the head office.

**Control Environment** The company maintains an adequate MIS which helps management to keep track of all operations and liaison with O&M operator.

### Operational Risk

**Power Purchase Agreement** Foundation Power's key source of earnings is the revenue generated through sale of electricity to the power purchaser, NTDC. 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. The term of the agreement is 25 years.

**Operation And Maintenance** Foundation Power Company has negotiated an O&M contract with KEPCO for a period of 18 years, signed in 2008. KEPCO, the O&M operator, ensures adherence of the plant to meet minimum performance benchmarks (Availability: Actual: 96.1%; Benchmark: 88%, Efficiency: Actual: 48.8%; Benchmark: 48.8%) during 1HFY19.

**Resource Risk** Foundation Power Company has negotiated the GSA with Mari Petroleum, for supply of 65mmcfcd of Low BTU Gas to the plant. The contract is for a period of 25 years. The construction and commissioning of the gas pipeline was completed in February 2009.

**Insurance Cover** Foundation Power has adequate insurance coverage for property damage and business interruption.

### Performance Risk

**Industry Dynamics** Pakistan total power generation is increasing on the back of new power projects under CPEC. Going forward, cheap renewable electricity will be a challenge to viability of thermal power plants. During FY18, there has been a growth of ~30% in the actual power generation. Moreover, there has been an increase of ~17% in the installed capacity as at end-Jun18 to 32,641MW (FY17: 27,731MW).

**Generation** Electricity generation stood at 663GWh, reduced by 2.4% during 1HFY19 as compare to 679GWh in 1HFY18 (FY18: 1,392GWh; FY17: 1,265GWh); a facet of lower electricity demand from the power purchaser. Moreover, electricity produced during 3QFY19 was 331GWh.

**Performance Benchmark** The required availability for Foundation Power under the PPA is 88%. During FY18, Foundation Power Daharki's efficiency and availability has been maintained according to agreed parameters. Meanwhile, the efficiency of the plant was 48.8% during FY18 (FY17: 48.8%); at par with the required benchmark of 48.8%, thus it made an operating profit of PKR 1,397mln during 1HFY19 (1HFY18: PKR 1,237mln, FY18: PKR 2,738mln, FY17: PKR 2,445mln).

### Financial Risk

**Financing Structure Analysis** Foundation Power's project cost (75%) was financed through a syndicated term finance loan. The loan size, PKR 11,565mln, is priced at 6-month KIBOR + 2.93% p.a., out of which PKR 3,794mln is outstanding as at end-Mar19. It is to be repaid in 20 unequal semi-annual installments. Seventeen installments have been made to date.

**Liquidity Profile** At end-Dec18, trade receivables of the company stood at PKR 8,502mln (FY18: PKR 6,785mln; FY17: PKR 4,925mln). As circular debt continues to be an issue for companies operating in power sector. Consequently, IPPs have to manage their liquidity requirements from internal cash generation and short-term borrowings.

**Working Capital Financing** A better working capital management is reflected from Foundation Power's financial statements. Increased trade payable days at 1HFY19: 314 days (end-FY18: 277 days; end-FY17: 189 days), leading to a negative cash cycle (1QFY19: -33 days; FY18: -31 days; FY17: -14 days). Constantly having negative cash cycle depicts the Co's strategy to align its receivable days with payable days while leaving available working capital lines un-utilized.

**Cash Flow Analysis** Despite reduced interest cost and increased cashflows, the company's coverages reflects slight decline in (FCFO post WC / Gross Interest + CMLTD + Uncovered STB: 1HFY19: 0.7x; FY18: 1.0x; FY17: 1.3x; FY16: 1.1x).

**Capitalization** Foundation Power has a moderately leveraged capital structure (Total Debt/Total Debt+Equity) as at end-Dec18 stood at 29.6% (FY18: 37.4%; FY17: 47.1%).



## Foundation Power Company Daharki Limited

PKR in mln

BALANCE SHEET	31-Dec-18	30-Jun-18	30-Jun-17	30-Jun-16
	6M	Annual	Annual	Annual
<b>Non-Current Assets</b>	<b>12,521</b>	<b>12,901</b>	<b>13,669</b>	<b>14,178</b>
<b>Current Assets</b>	<b>8,937</b>	<b>7,595</b>	<b>5,594</b>	<b>5,379</b>
Inventory	34	34	34	37
Trade Receivables	8,502	6,785	4,925	4,169
Other Current Assets	374	365	375	585
Cash & Bank Balances	27	412	261	588
<b>Total Assets</b>	<b>21,458</b>	<b>20,497</b>	<b>19,263</b>	<b>19,557</b>
<b>Debt</b>	<b>3,789</b>	<b>5,045</b>	<b>6,506</b>	<b>8,230</b>
Short-term	-	-	50	464
Long-term (Incl. Current Maturity of long-term debt)	3,789	5,045	6,456	7,766
Other Short term liabilities (inclusive of trade payables)	8,577	6,948	5,375	4,657
Other Long term Liabilities	1,402	1,407	1,455	1,535
<b>Shareholder's Equity</b>	<b>7,690</b>	<b>7,097</b>	<b>5,928</b>	<b>5,135</b>
<b>Total Liabilities &amp; Equity</b>	<b>21,458</b>	<b>20,497</b>	<b>19,263</b>	<b>19,557</b>

## INCOME STATEMENT

<b>Turnover</b>	<b>5,519</b>	<b>10,060</b>	<b>10,259</b>	<b>11,235</b>
Gross Profit	1,470	2,929	2,612	3,118
Other Income	19	31	53	63
Financial Charges	(295)	(672)	(818)	(1,019)
<b>Net Income</b>	<b>1,122</b>	<b>2,088</b>	<b>1,689</b>	<b>1,990</b>

## Cashflow Statement

Free Cashflow from Operations (FCFO)	1,772	3,495	3,206	3,695
Net Cash changes in Working Capital	(145)	(380)	49	(1,227)
Net Cash from Operating Activities	1,393	2,817	2,555	1,544
Net Cash from Investing Activities	17	27	(157)	(24)
Net Cash from Financing Activities	(1,794)	(2,693)	(2,733)	(1,944)
Net Cash generated during the period	(384)	151	(335)	(424)

## Ratio Analysis

<b>Performance</b>				
Turnover Growth	17.1%	-1.9%	-8.7%	-5.3%
Gross Margin	26.6%	29.1%	25.5%	27.8%
Net Margin	20.3%	20.8%	16.5%	17.7%
ROE	24.8%	24.7%	23.1%	30.0%
<b>Coverages</b>				
FCFO Pre-WC/Gross interest+CMLTD	0.8	1.1	1.3	1.6
FCFO Post-WC/Gross interest+CMLTD	0.7	1.0	1.3	1.1
<b>Liquidity</b>				
Net Cash Cycle	-32.7	-30.6	-14.0	-16.8
<b>Capital Structure</b>				
Net Debt/Net Debt+Equity	29.6%	37.4%	47.1%	55.4%

## Foundation Power Company Daharki Limited

Apr-19

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## Credit Rating Scale & Definitions

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.

Long Term Ratings		Short Term Ratings	
<b>AAA</b>	<b>Highest credit quality.</b> Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments	<b>A1+</b>	The highest capacity for timely repayment.
<b>AA+</b> <b>AA</b> <b>AA-</b>	<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.	<b>A1</b>	A strong capacity for timely repayment.
<b>A+</b> <b>A</b> <b>A-</b>	<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.	<b>A2</b>	A satisfactory capacity for timely repayment. This may be susceptible to adverse changes in business, economic, or financial conditions.
<b>BBB+</b> <b>BBB</b> <b>BBB-</b>	<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.	<b>A3</b>	An adequate capacity for timely repayment. Such capacity is susceptible to adverse changes in business, economic, or financial conditions.
<b>BB+</b> <b>BB</b> <b>BB-</b>	<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.	<b>B</b>	The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions.
<b>B+</b> <b>B</b> <b>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>C</b>	An inadequate capacity to ensure timely repayment.
<b>CCC</b> <b>CC</b> <b>C</b>	<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.		
<b>D</b>	Obligations are currently in default.		



**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, a) some material identifiable event and/or b) deviation from expected trend. 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 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) cessation of underlying entity, c) the debt instrument is redeemed, d) the rating remains suspended for six months, e) the entity/issuer defaults, or/and f) 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.

**Disclaimer:** PACRA's ratings are an assessment of the credit standing of entities/issue in Pakistan. They do not take into account the potential transfer / convertibility risk that may exist for foreign currency creditors. PACRA's opinion is not a recommendation to purchase, sell or hold a security, in as much as it does not comment on the security's market price or suitability for a particular investor.

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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**

- 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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- (3) No director, officer or employee of PACRA communicates the information, acquired by him for use for rating purposes, to any other person except where required under law to do so. | Chapter III; 10-(5)
- (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)

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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.
- (8) PACRA prohibits its employees and analysts from soliciting money, gifts or favors from anyone with whom PACRA conducts business | Chapter III; 11-A-(q)
- (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)
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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)
- (14) PACRA discloses that no shareholder directly or indirectly holding 10% or more of the share capital of PACRA also holds directly or indirectly 10% or more of the share capital of the entity which is subject to rating or the entity which issued the instrument subject to rating by PACRA; | Reference Chapter III; 12-2-(f)
- (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)
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- (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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