

RATING REPORT

Neelum Jhelum Hydropower Company (Private) Limited

REPORT DATE:

January 20, 2019

RATING ANALYSTS:

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RATING DETAILS

Rating Category	Instrument Rating	
	Long-term	Long-term
Sukuk	AAA	AAA
Rating Date	Dec '24'2019	Jan'02'2019
Rating Outlook	Stable	Stable

COMPANY INFORMATION

Incorporated in 2004

External auditors: Ernst & Young Ford Rhodes Sidat Hyder

Private Limited Company

Chairman of the Board: Lt. Gen (Retd) Muzammil Hussain

Key Shareholders (with stake 5% or more):

Chief Executive Officer: Brig (Retd) Muhammad Zareen

WAPDA (Water & Power Development Authority) – 99%

APPLICABLE METHODOLOGY(IES)

VIS Entity Rating Criteria: Industrial Corporate (May 2019)

Notching The Issue (June 2016)

<https://www.vis.com.pk/kc-meth.aspx>

Neelum Jhelum Hydropower Company (Private) Limited

OVERVIEW OF THE INSTITUTION

Neelum Jhelum Hydropower Company (Private) Limited (NJHPC) was incorporated on November 18, 2004. The company is a Special Purpose Vehicle (SPV) constituted as a subsidiary of WAPDA (Water and Power Development Authority) for the generation and sale of electricity via the development of Neelum Jhelum Hydropower Power project (NJHPP).

Profile of Chairman

Lt. Gen. (Retd.) Muzammil Hussain, HI (Mil) assumed charge as Chairman of WAPDA on August 24, 2016. He carries over 38 years of experience in Armed forces and is a graduate from Pakistan Military Academy (PMA) with distinction.

Profile of CEO

Brig (Retd.) Muhammad Zareen has been appointed as CEO of NJHPC in September, 2016. Previously, he has served as *Advisor* Northern Area Projects and General Manager Projects (Northern Areas) for WAPDA.

Financial Snapshot

Net Equity: FY19: Rs. 99.2b; FY18: Rs. 100.4b; FY17: Rs. 96.1b;
Total Assets: FY19: Rs. 479.6b; FY18: Rs. 463.5b; FY17: Rs. 376.5b

RATING RATIONALE

The rating assigned to the Sukuk issue take into account unconditional and irrevocable first demand guarantee issued by the President Islamic Republic of Pakistan (on behalf of the Government of the Islamic Republic of Pakistan) (GoP) covering issue amount of the Sukuk along with profit payments. GoP would immediately pay the entire called amount once the demand notice from the trustee is received. Ratings also incorporate strong financial muscle and implicit support from the parent entity, Water and Power Development Authority (WAPDA), in the form of equity injection and funding support.

Physical progress stands at 99.56%: NJHPC was setup to design, construct, own, operate and maintain Neelum Jhelum Hydropower Power Project (NJHPP) which is a state-of-the-art, world class underground facility with installed capacity of 969 MW. The main purpose is the development of NJHPP for generation and sale of electricity to CPPAG. It is a Composite Dam (Gravity + Rock fill) having height of 60 meters, comprising four Turbines of 242.25 MW each. All four units were operational during FY19; however generation capacity of the power plant is directly linked to the availability of water; therefore the energy has a sizeable seasonal variation. The total generation of unit I, II, III and IV was recorded at 100.2m kWh, 6.1m kWh, 121.5m kWh and 343.3m kWh respectively at end-Sep'19. As per the management, the company has provided around 6.1b kWh to the national grid by 20th Nov'19. The other three main components include a dam, water-way system with 52 km long tunnels, and an underground power house. The transmission lines, powerhouse and switch yard have also achieved completion. Physical progress stands at 99.56%, as per the latest progress report of the project. In aggregate, the Neelum-Jhelum project will provide about 5 billion units of low-cost hydel electricity to the national grid every year. Annual benefits of the project have been estimated at Rs. 55 billion per annum. In addition, the delay in COD and related cost overruns are likely to be compensated by inclusion of the same in the proposed tariff structure.

The tariff structure has not yet been finalized: As per the 4th revision in PC-1 2017, the approved contract cost was approved at Rs. 506.8 billion; however, as per the management the project is expected to be completed within Rs. 430.0 billion with cost amounting to Rs. 421 billion at end-Sep'19. The project cost is being funded through a debt: equity: grant ratio of 79:10:11 with grant component covered by the Neelum-Jhelum surcharge. The government imposed a 10 paisa / unit surcharge in FY07 which has since been extended in line with the cost escalation. NEPRA determined provisional tariff of Rs. 5.91 kWh for one year in Nov'18 which was notified by the government on 13th March'19. The provisional tariff was unacceptable to NJHPC therefore the company filed review petition before NEPRA. The revised provisional tariff of Rs. 9.12 kWh was announced on 19th August'19 which included components of debt repayment and operations & maintenance; however the components of insurance, water use surcharge and profitability will be added once the final tariff is decided. No invoice on account of sale of power has been raised so far due to non-signing of Power Purchase agreement (PPA) with CPPA-G, discussions are in progress for signing of PPA. Invoice will be raised with arrears once PPA is signed between NJHPC and CPPA-G. As per the management the final tariff is expected to be around Rs. 14.0/ kWh; the same is likely to be finalized after the company achieves official commercial operations, the timeline for the same is March'2020. Final tariff approval by NEPRA will be crucial to the debt servicing

capacity of the company. A contractual asset was recorded on the company's balance sheet amounting to Rs. 36.1b during FY19 on account of unearned revenue amounting to 27.8b coupled with revenue from trail production adjusted from capital work in progress.

The Sukuk is an unlisted, privately placed and non-SLR eligible. It has a tenor of 10 years inclusive of a grace period of 2 years beginning from first drawdown of the Sukuk. First drawdown of Rs. 30b occurred in June'2016; second drawdown of Rs. 35b at end-Oct'16 and the third drawdown of Rs. 35b was completed by end-June'18. The profit rate on the Sukuk is payable semi-annually and is equivalent to 6-month KIBOR +175bps; however, NJHPP is entitled to a rebate of up to 62bps in case payment is made within 30 days of the due date. The first payment amounting to Rs. 10.3b including principal payment of Rs. 6.25b was made on December 29, 2018; meanwhile the second installment amounting to Rs. 11.8b was made on June 29, 2019. As per the waterfall mechanism, an amount equivalent to one-sixth of the installment amount is being deposited each month so that debt payment account (DPA) on the installment date is equivalent to the installment amount. In case of any shortfall in DPA by NJHPC, WAPDA will inject the required funds. In the absence of any income stream, DPA is being recharged with the borrowed amount. As per the management, DPA has been filled with the required amount to be paid on the due date.

Despite increase in Government Grant (NJ-Surcharge) to 65.6b (FY18: Rs. 58.6b) the equity base of the company decreased marginally to Rs. 99.2b (FY18: 100.4b; FY17: Rs. 96.1b) by end-FY19 mainly as a result of higher accumulated loss reported in line with finance cost and depreciation charge amounting to Rs. 26.8b and Rs. 8.4b incurred respectively during FY19. The remaining equity has been contributed by WAPDA. The long-term funding also increased by end-FY19 on account of additional loan procured from Exim Bank China, Islamic Development Bank and OPEC Fund for International Development for capital expenditure and to retire Sukuk payment due in Jun'19.

Neelum-Jhelum Hydropower Company (NJHPC)
Appendix I

BALANCE SHEET	FY17	FY18	FY19
Operating Fixed Assets	1,043.5	1,128.1	-
Capital Work in Progress	338,274.4	402,023.9	404,317.0
Other Non-Current Assets	1,877.1	1,797.4	335.6
Other Current Assets	442.0	299.7	553.0
Contact Asset	-	-	36,147.1
Bank Balances	34,826.1	58,261.5	38,230.8
TOTAL ASSETS	376,463.1	463,510.6	479,583.3
EQUITY			
Issued, subscribed and paid up capital	41,663.5	41,663.5	41,663.5
Accumulated Profit/(Loss)	(2,092.3)	(5,202.6)	(13,402.1)
Share Deposit Money	5,300.0	5,300.0	5,300.0
Government Grant (NJS)	51,213.6	58,593.4	65,616.2
LIABILITIES			
Long-Term Financing	133,688.7	156,051.9	169,034.0
NBP Sukuk	65,000.0	100,000.0	87,500.0
Retention Money Payable	12,002.9	9,958.7	6,683.4
Current Liabilities	69,686.7	106,332.5	139,218.7
Current Ratio (x)	0.43	0.45	0.47
Debt to Equity (x)	N/A	N/A	N/A
TOTAL EQUITY & LIABILITIES	376,463.1	463,510.6	479,583.3
INCOME STATEMENT	FY17	FY18	FY19
Revenue	-	-	27,797.6
Gross Profit	-	-	18,764.0
Administration Expenses	1.8	43.4	63.9
Finance Cost	-	-	1,502.7
Profit/ (Loss) Before Tax	(1,804.0)	(1,748.0)	(9,561.7)
Net Profit/(Loss)	(1,804.0)	(3,110.2)	(8,199.5)

ISSUE/ISSUER RATING SCALE & DEFINITIONS

Appendix II

VIS Credit Rating Company Limited

RATING SCALE & DEFINITIONS: ISSUES / ISSUERS

Medium to Long-Term

AAA

Highest credit quality; the risk factors are negligible, being only slightly more than for risk-free Government of Pakistan's debt.

AA+, AA, AA-

High credit quality; Protection factors are strong. Risk is modest but may vary slightly from time to time because of economic conditions.

A+, A, A-

Good credit quality; Protection factors are adequate. Risk factors may vary with possible changes in the economy.

BBB+, BBB, BBB-

Adequate credit quality; Protection factors are reasonable and sufficient. Risk factors are considered variable if changes occur in the economy.

BB+, BB, BB-

Obligations deemed likely to be met. Protection factors are capable of weakening if changes occur in the economy. Overall quality may move up or down frequently within this category.

B+, B, B-

Obligations deemed less likely to be met. Protection factors are capable of fluctuating widely if changes occur in the economy. Overall quality may move up or down frequently within this category or into higher or lower rating grade.

CCC

Considerable uncertainty exists towards meeting the obligations. Protection factors are scarce and risk may be substantial.

CC

A high default risk

C

A very high default risk

D

Defaulted obligations

Short-Term

A-1+

Highest certainty of timely payment; Short-term liquidity, including internal operating factors and /or access to alternative sources of funds, is outstanding and safety is just below risk free Government of Pakistan's short-term obligations.

A-1

High certainty of timely payment; Liquidity factors are excellent and supported by good fundamental protection factors. Risk factors are minor.

A-2

Good certainty of timely payment. Liquidity factors and company fundamentals are sound. Access to capital markets is good. Risk factors are small.

A-3

Satisfactory liquidity and other protection factors qualify entities / issues as to investment grade. Risk factors are larger and subject to more variation. Nevertheless, timely payment is expected.

B

Speculative investment characteristics; Liquidity may not be sufficient to ensure timely payment of obligations.

C

Capacity for timely payment of obligations is doubtful.

Rating Watch: VIS places entities and issues on 'Rating Watch' when it deems that there are conditions present that necessitate re-evaluation of the assigned rating(s). Refer to our 'Criteria for Rating Watch' for details. www.vis.com.pk/images/criteria_watch.pdf

Rating Outlooks: The three outlooks 'Positive', 'Stable' and 'Negative' qualify the potential direction of the assigned rating(s). An outlook is not necessarily a precursor of a rating change. Refer to our 'Criteria for Rating Outlook' for details. www.vis.com.pk/images/criteria_outlook.pdf

{SO} Rating: A suffix (SO) is added to the ratings of 'structured' securities where the servicing of debt and related obligations is backed by some sort of financial assets and/or credit support from a third party to the transaction. The suffix (SO), abbreviated for 'structured obligation', denotes that the rating has been achieved on grounds of the structure backing the transaction that enhanced the credit quality of the securities and not on the basis of the credit quality of the issuing entity alone.

{blr} Rating: A suffix (blr) is added to the ratings of a particular banking facility obtained by the borrower from a financial institution. The suffix (blr), abbreviated for 'bank loan rating' denotes that the rating is based on the credit quality of the entity and security structure of the facility.

'p' Rating: A 'p' rating is assigned to entities, where the management has not requested a rating, however, agrees to provide informational support. A 'p' rating is shown with a 'p' subscript and is publicly disclosed. It is not modified by a plus (+) or a minus (-) sign which indicates relative standing within a rating category. Outlook is not assigned to these ratings. Refer to our 'Policy for Private Ratings' for details. www.vis.com.pk/images/policy_ratings.pdf

'SD' Rating: An 'SD' rating is assigned when VIS believes that the ratee has selectively defaulted on a specific issue or obligation but it will continue to meet its payment obligations on other issues or obligations in a timely manner.

REGULATORY DISCLOSURES		Appendix III			
Name of Rated Entity	Neelum Jhelum Hydropower Company (Private) Limited				
Sector	Power				
Type of Relationship	Solicited				
Purpose of Rating	Sukuk rating				
Rating History	Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
	<u>RATING TYPE: ENTITY</u>				
	24/12/2019	AAA	N/a	Stable	Reaffirmed
	2/01/2019	AAA	N/a	Stable	Reaffirmed
	13/09/2017	AAA	N/a	Stable	Reaffirmed
	12/04/2016	AAA	N/a	Stable	Preliminary
Instrument Structure	Apart from GoP guarantee, security structure of the Sukuk entails charge on all unencumbered present and future assets of the company and exclusive lien over debt payment account (DPA). As per the waterfall mechanism, an amount equivalent to one-sixth of the installment amount will be deposited each month so that DPA on the installment date is equivalent to the installment amount. In case of any shortfall in DPA Account by NJHPC, WAPDA will inject the required funds.				
Statement by the Rating Team	VIS, the analysts involved in the rating process and members of its rating committee do not have any conflict of interest relating to the credit rating(s) mentioned herein. This rating is an opinion on credit quality only and is not a recommendation to buy or sell any securities.				
Probability of Default	VIS ratings opinions express ordinal ranking of risk, from strongest to weakest, within a universe of credit risk. Ratings are not intended as guarantees of credit quality or as exact measures of the probability that a particular issuer or particular debt issue will default.				
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Due Diligence Meetings Conducted		Name	Designation	Date	
	1	Mr. Hamid Mahmood	CFO	21-Nov-2019	