The Pakistan Credit Rating Agency Limited

AZM CERTIFICATES – TFC III
ISSUER: K-ELECTRIC LIMITED

TFCs Issue (Secured, Listed)	NEW [MAR-16]	PREVIOUS [JUN-15]
TFC III	AA+	AA+
Outlook	Stable	Stable

REPORT CONTENTS

MARCH 2016

Issuer Profile

- K-Electric (KE), is involved in generation, transmission and distribution of electricity in Karachi and its adjoining areas
- The company is ~66% owned by KES Power Limited (KESP), while GoP holds 24% stake; holding company – KESP – is majority owned (~52%) by Abraaj Capital (a Private Equity Investor)
- Thirteen member board comprises nine representatives of KESP, three GoP members and one independent member
- The CEO – Mr. Tayyab Tareen – is supported by a team of experienced professionals

Instrument Structure

- KE, for the purpose of meeting its working capital requirements, issued three Secured, Rated, Listed TFCs having tenors of 13, 36, and 60 months respectively in Aug-12 with total issue size of PKR 2,000mln
- TFC I (PKR 300mln), and TFC II (PKR 1,200mln) redeemed in Sep13 and Aug15, respectively; TFC III (PKR 500mln) will be redeemed in Aug17
- TFC (III) carry a put option which is subject to service the extent of which varies according to the lapsed time; to cater to this risk KE has to keep unutilized line of PKR 1bln. Unutilized line at end-Feb16 stand was PKR 1bln
- TFC holders are repaid through collections emanating from specific (carved out) consumers. The security is categorized in two classes:
  (i) First parri passu charge on designated receivables from specific 250 corporate consumers (core) being the amounts paid or to be paid by them to KE under the consumer bills. Receivables are being shared on pari passu basis with Financing Facility of up to PKR 3,000mln being obtained by KE; no additional charge can be created
  (ii) First parri passu charge on another set of 495 specific entities (additional). A new PKR 22bln Sukuk with a grace period of 2 years was issued in FY15; Sukuk also have a first parri passu charge on receivables along with Syndicated Term Facility loan of PKR 7.7bln
- Entrapment of funds in Debt Payment Account (DPA) for each quarter is done, on an equal monthly basis starting three months prior to the due date; DPA is maintained at a minimum 1.2x throughput margin (interest due plus required principal) for any given quarter throughout the tenor of the issue

Assessment

- The ratings are assigned on the basis of forecasted coverages which are expected to remain strong over the tenor of the TFC
- Forecasting methodology entails calculation of cashflows – minimum and average – vis-a-vis required build-up based on (i) monthly consumption by carved out consumers, (ii) average tariff, and (iii) collection ratio
- Payments on the financing facility and Sukuk were incorporated while calculating actual and future coverage's
- Minimum monthly consumption to project future monthly inflows captures effect of seasonality as well as low demand levels; credit risk is mitigated to a large extent by taking the minimum collection ratio and a diverse sectoral distribution of carved out consumers
- Since the issuance of TFCs actual minimum coverage during 42 months (Aug12 – Jan16) for specific 250 and 495 consumers stood at 2.2x and 5.1x, respectively against minimum requirement of 1.2x
- Forecasted minimum coverage stood at 2.4x and 2.2x for specific 250 and 495 consumers, respectively

RATING RATIONALE

The ratings reflect demonstrated history of timely repayments of outstanding retail TFCs - Azm - issued by KE. Strong security structure of instrument outline that TFC holders have a first pari passu charge on bills receivable from two sets (core and additional) of carved out consumers. The bill collection ratio of these sets is strong. A minimum throughput of 1.2x is to be maintained from receivables of carved out consumers - 250 specific entities (core) and 495 specific entities (additional). The amounts received are directly deposited into Debt Payment Account (DPA), which is gradually built over a period prior to each repayment date to avoid pressure on any single month. Historical pattern of collections is robust and hence, cashflow coverages are expected to remain strong. Meanwhile, coverages since the issuance of the instrument have been stronger than expected. This is attributable to good collection pattern, and increase in underlying revenues. Out of the series of TFCs issue, KE has successfully redeemed TFC (I) and TFC (II) in Sep13 and Aug15 as per agreed timelines. Volatile domestic socio-political environment may exert some pressure on the issuer though its impact on TFCs performance is expected to remain limited.

KEY RATING DRIVERS

The ratings are dependent on the continued compliance with the predefined security structure of the instrument. Moreover, any significant deterioration in the performance of KE, impacting the projected collection stream, would have negative implications for the rating though the likelihood of this is remote.

Actual and Forecasted Coverages

Actual

	Receivable From:											
	250 Corporate Customers (Standalone)					495 MCA Customers (Excess)						
Date	Buildup Required (PKR mln)	Minimum Monthly Bills Received (PKR mln)	Coverage	Average Monthly Bill Received (PKR mln)	Coverage	Buildup Required (PKR mln)	Minimum Monthly Bills Received (PKR mln)	Coverage	Average Monthly Bill Received (PKR mln)	Coverage	Total Minimum Coverage	Total Average Coverage
Jul-12	26	333	12.6	333	12.6	26	1,816	69.0	1,816	69.0	82	82
Aug-12	116	347	3.0	347	3.0	26	1,933	73.4	1,933	73.4	76	76
Sep-12	138	391	2.8	391	2.8	48	1,988	41.7	1,988	41.7	45	45
Oct-12	138	401	2.9	401	2.9	48	1,795	37.7	1,795	37.7	41	41
Nov-12	136	389	2.9	389	2.9	48	1,686	35.4	1,686	35.4	38	38
Dec-12	136	356	2.6	356	2.6	48	1,590	33.4	1,590	33.4	36	36
Jan-13	136	313	2.3	313	2.3	48	1,581	33.2	1,581	33.2	35	35
Feb-13	134	338	2.5	338	2.5	48	1,626	34.1	1,626	34.1	37	37
Mar-13	134	324	2.4	324	2.4	48	1,538	32.3	1,538	32.3	35	35
Apr-13	134	377	2.8	377	2.8	48	1,781	37.4	1,781	37.4	40	40
May-13	132	326	2.5	326	2.5	48	1,675	35.2	1,675	35.2	38	38
Jun-13	131	435	3.3	435	3.3	47	1,747	37.5	1,747	37.5	41	41
Jul-13	131	375	2.9	375	2.9	47	1,723	37.0	1,723	37.0	40	40
Aug-13	105	383	3.6	383	3.6	23	1,802	76.8	1,802	76.8	80	80
Sep-13	103	646	6.3	646	6.3	21	2,655	124.6	2,655	124.6	131	131
Oct-13	103	578	5.6	578	5.6	21	2,482	116.5	2,482	116.5	122	122
Nov-13	101	512	5.1	512	5.1	21	2,422	113.7	2,422	113.7	119	119
Dec-13	101	585	5.8	585	5.8	21	2,469	115.9	2,469	115.9	122	122
Jan-14	101	522	5.2	522	5.2	21	2,454	115.2	2,454	115.2	120	120
Feb-14	99	501	5.0	501	5.0	21	2,408	113.1	2,408	113.1	118	118
Mar-14	99	533	5.4	533	5.4	21	2,499	117.4	2,499	117.4	123	123
Apr-14	99	579	5.8	579	5.8	21	2,710	127.3	2,710	127.3	133	133
May-14	97	622	6.4	622	6.4	41	2,813	69.2	2,813	69.2	76	76
Jun-14	97	624	6.4	624	6.4	62	2,971	48.2	2,971	48.2	55	55
Jul-14	97	568	5.8	568	5.8	47	2,818	59.5	2,818	59.5	65	65
Aug-14	95	510	5.4	510	5.4	47	2,477	52.3	2,477	52.3	58	58
Sep-14	195	605	3.1	605	3.1	147	2,822	19.2	2,822	19.2	22	22
Oct-14	195	568	2.9	568	2.9	156	2,777	17.9	2,777	17.9	21	21
Nov-14	193	584	3.0	584	3.0	156	2,603	16.7	2,603	16.7	20	20
Dec-14	193	563	2.9	563	2.9	156	2,644	17.0	2,644	17.0	20	20
Jan-15	193	453	2.3	453	2.3	198	2,235	11.3	2,235	11.3	14	14
Feb-15	191	449	2.3	449	2.3	198	2,111	10.7	2,111	10.7	13	13
Mar-15	191	429	2.2	429	2.2	198	2,069	10.5	2,069	10.5	13	13
Apr-15	191	533	2.8	533	2.8	188	2,370	12.6	2,370	12.6	15	15
May-15	189	644	3.4	644	3.4	188	2,970	15.8	2,970	15.8	19	19
Jun-15	189	585	3.1	585	3.1	188	2,771	14.7	2,771	14.7	18	18
Jul-15	189	493	2.6	493	2.6	324	2,539	7.8	2,539	7.8	10	10
Aug-15	187	519	2.8	519	2.8	324	2,342	7.2	2,342	7.2	10	10
Sep-15	72	597	8.2	597	8.2	209	2,852	13.6	2,852	13.6	22	22
Oct-15	72	548	7.6	548	7.6	426	2,539	6.0	2,539	6.0	14	14
Nov-15	70	541	7.7	541	7.7	426	2,448	5.7	2,448	5.7	13	13
Dec-15	70	439	6.2	439	6.2	426	2,185	5.1	2,185	5.1	11	11
Jan-16	70	473	6.7	473	6.7	403	2,236	5.6	2,236	5.6	12	12
Feb-16	56	405	7.2	471	8.3	403	2,124	5.3	2,389	5.9	12	14
Mar-16	56	422	7.5	482	8.5	403	2,157	5.4	2,428	6.0	13	15
Apr-16	6	450	69.5	526	81.2	426	2,352	5.5	2,612	6.1	75	87
May-16	6	397	61.3	544	84.1	426	2,314	5.4	2,691	6.3	67	90
Jun-16	6	455	70.4	571	88.3	426	2,409	5.7	2,848	6.7	76	95
Jul-16	6	407	62.9	504	77.9	438	2,065	4.7	2,726	6.2	68	84
Aug-16	6	456	70.5	509	78.7	438	2,045	4.7	2,729	6.2	75	85
Sep-16	6	458	71.1	547	85.0	438	1,790	4.1	2,672	6.1	75	91
Oct-16	6	411	63.8	497	77.3	431	2,110	4.9	2,421	5.6	69	83
Nov-16	6	516	80.1	555	86.2	431	2,073	4.8	2,458	5.7	85	92
Dec-16	6	424	65.9	523	81.2	431	2,160	5.0	2,466	5.7	71	87
Jan-17	6	347	53.9	434	67.4	424	1,964	4.6	2,291	5.4	59	73
Feb-17	6	405	62.9	471	73.2	424	2,124	5.0	2,389	5.6	68	79
Mar-17	6	422	65.6	482	74.9	424	2,157	5.1	2,428	5.7	71	81
Apr-17	6	450	70.0	526	81.7	418	2,352	5.6	2,612	6.2	76	88
May-17	6	397	61.7	544	84.6	418	2,314	5.5	2,691	6.4	67	91
Jun-17	172	455	2.6	571	3.3	584	2,409	4.1	2,848	4.9	7	8
Jul-17	172	407	2.4	504	2.9	938	2,065	2.2	2,726	2.9	5	6
Aug-17	172	456	2.6	509	3.0	938	2,045	2.2	2,729	2.9	5	6

STANDARD 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

AAA	**Highest credit quality.** Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments. This capacity is highly unlikely to be adversely affected by foreseeable events.
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-	**Speculative.** Possibility of credit risk developing. There is a possibility of credit risk developing, particularly as a result of adverse economic change over time; however, business or financial alternatives may be available to allow financial commitments to be met.
B+ B B-	**Highly speculative.** Significant 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	**High default 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.

SHORT TERM RATINGS

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.

B: The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions.

C: An inadequate capacity to ensure timely repayment.

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. Rating Watch may carry designation – Positive (rating may be raised, negative (lowered), or developing (direction is unclear). A watch should be resolved with in foreseeable future, but may continue if underlying circumstances are not settled.

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'.

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, or e) the entity/issuer defaults.

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Name of Issuer K-Electric
Name of Issue Azm Certificate - TFC III
Sector Energy | Utilities
Type of Relationship Solicited

Purpose of the Rating Independent Risk Assessment

Rating History

Notification Date	TFC Rating	Outlook	Action
30-Mar-16	AA+	Stable	Maintained
5-Jun-15	AA+	Stable	Upgrade
13-Jun-14	AA	Stable	Maintained
3-Apr-13	AA	Stable	Maintained
5-Jun-12	AA	Stable	Initial

Instrument Details

Nature of Instrument	Size of Issue	Tenor	Trustee	Security
TFC (Lsited)	PKR 500mln	5 years	Pak Brunei Investment Company Limited	- Secured - First parri passu charge on designated receivables of 250 corporate consumers - First parri passu charge on another 495 specific entities

Related Criteria and Research

Rating Methodology: Debt Instrument Rating Methodology

Amortization Schedule: See Annexure A

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Rating Team Statement

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Probability of Default (PD)

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

Repayment Schedule TFC-III Annexure A

TFC Amount (PKR mln)	500
Period (years)	5
Principal Repayment	Aug-17
Interest payment	Quarterly
Pricing	15.50%

Date	Installment	Beginning Principal	Payment Principal	Payment Markup	Ending Principal
12-Aug-12		500	-	-	500
30-Aug-12		500		14	500
12-Nov-12	19	500	0	19	500
12-Feb-13	19	500	0	19	500
12-May-13	19	500	0	19	500
12-Aug-13	19	500	0	19	500
12-Nov-13	19	500	0	19	500
12-Feb-14	19	500	0	19	499
12-May-14	19	499	0	19	499
12-Aug-14	19	499	0	19	499
12-Nov-14	19	499	0	19	499
12-Feb-15	19	499	0	19	499
12-May-15	19	499	0	19	499
12-Aug-15	19	499	0	19	499
12-Nov-15	19	499	0	19	499
12-Feb-16	19	499	0	19	499
12-May-16	19	499	0	19	499
12-Aug-16	19	499	0	19	498
12-Nov-16	19	498	0	19	498
12-Feb-17	19	498	0	19	498
12-May-17	19	498	0	19	498
12-Aug-17	517	498	498	19	-
	901		**500**	**401**	