



The Pakistan Credit Rating Agency Limited

SUI SOUTHERN GAS COMPANY LIMITED

	NEW [JUN-16]	PREVIOUS [JUN-15]	REPORT CONTENTS
Long-Term	A+	AA-	1. RATING ANALYSES
Short-Term	A1	A1	2. FINANCIAL INFORMATION
Outlook	Rating Watch (-ve)	Rating Watch (-ve)	3. RATING SCALE
			4. REGULATORY AND SUPPLEMENTARY DISCLOSURE

JUNE 2016

Profile & Ownership

- SSGC, formed in 1989, is engaged in the business of the purchase, transmission, and distribution of natural gas
- Operating with a transmission and distribution network of 49,276km, SSGC serves ~2.8mln customers across Sindh and Balochistan
- Owns and operates gas meter manufacturing plant; annual capacity of 750,000 meters
- SSGC is majority (~67%) owned by Government of Pakistan including 13% through public sector companies and corporations

Governance

- Thirteen-members board including the MD; Seven Government nominees, four independent directors, while one each represent SLIC and NIT
- Board members possess good mix of skill set; risk of political intervention remains

Management and Operational Risk

- Mr. Khalid Rahman joined as MD in Jan15; frequent changes at top management were witnessed in the past
- Tall organization structure; adequately long associated and experienced management team
- Operational infrastructure requires regular capital expenditure
- Deploys oracle based ERP; comprehensive MIS reporting mechanism

Performance

- In Nov15, OGRA approved Final Revenue Requirements for three years; FY13 to FY15
- The company enjoys legal stay on UFG benchmark of 7% versus OGRA allowed 4.5% till UFG study and subsequent Sindh High Court decision
- Partial UFG volume in law and order and pilfered volume by non-consumer was provisionally allowed; thus, provided some respite
- Net operating assets witnessed nominal increase (~3%) during FY15, leading to minimal increase in guaranteed returns on YoY basis
- Increase in UFG losses (FY15: 13.6%, FY14: 13.8%) translated into higher UFG disallowance (FY15: PKR 10,282mln; FY14: PKR 9,944mln). The company reported higher loss before tax (FY15: PKR 8.8bln; FY14: PKR 5.8bln) on YoY basis
- An adverse decision from SHC regarding UFG benchmark would significantly impact company's bottom-line, in turn, would erode equity
- SSGC is presently in process of laying down gas pipelines for LNG in two phases. Phase-1 (14KM: cost PKR 2.3bln) is completed and Phase-II (338KM pipeline along with ancillary equipment: cost PKR 58bln, expected completion Dec16) is underway
- SSGC has filed petition with OGRA for inclusion of LNG project assets in net operating asset base; this will significantly increase the guaranteed return upon completion of the project

Financial Risk

- In recent years, the circular debt issue has weakened the liquidity position as the receivables surged; working capital managed by delaying payments to gas suppliers resulting in an increase in trade payables
- Coverages are below adequate level
- Significant asset-liability mismatch at end-Jun15: PKR 31bln (end-Jun14: PKR 19bln)
- High leveraging due to debt driven CAPEX projects. Weak operational performance in recent years reduced equity, in turn, higher leveraging (debt to debt plus equity ratio: end-Jun15: ~61%, end-Jun14: 54%)
- Going forward, debt level is expected to increase significantly (upto PKR 75bln: ~PKR 39bln carries government guarantee) owing to debt financed LNG projects

RATING RATIONALE

In Nov15, OGRA - the regulator - finalized the longstanding revenue requirements (FRR) for SSGC. OGRA, while determining its benchmark rate for Unaccounted For Gas (UFG) losses at 7% - on the basis of interim relief given by Sindh High Court - also allowed certain allowances in line with the Economic Coordination Committee guidelines. Consequently, SSGC has issued its long overdue financial statements (FY13-FY15). However, the timeliness of financial statement is yet to fully regularize (quarterly financials of FY16 are delayed).

Given SSGC's exclusive license to operate in its area of franchise (provinces of Sindh and Balochistan) and guaranteed return on its net operating assets, the business profile is considered strong. However, the company's profitability has been significantly impacted on account of UFG losses. Nevertheless, provisional allowance of certain claims regarding UFG volume in law affected areas and pilfered volume by non-consumer by OGRA has provided some relief. The company's financial risk profile is stretched owing to (i) high leveraging - a factor of debt-driven CAPEX projects, and (ii) inadequate coverages - due to lower cashflows. Working capital requirement (gaps in inflows from consumers and the government), a continuous drag on the liquidity profile, is managed through holding payables to state-owned gas suppliers; consequently, limited related borrowings. SSGC is a part of Re-gasified Liquid Natural Gas (RLNG) project. Under the project, SSGC will be laying 338KMs pipeline at an estimated cost of ~PKR 39bln; expected commissioning: Dec16. The loan carries a sovereign guarantee with repayments commencing in Jun18. Return on these new assets should support SSGC's diminished profitability. Consequent cashflows should also provide some respite to financial risk profile in the medium term. The ratings continue to draw material comfort from sovereign ownership structure and forthcoming support from GoP in case the need arises.

KEY RATING DRIVERS

The company enjoys legal stay on UFG benchmark of 7% versus OGRA allowed 4.5%. Final resolution of the matter is pending till completion of UFG impact study and subsequent decision by Sindh High Court. The negative outlook captures the downside, which, if materializes, will have significant detrimental impact on the profile of the company. Notably, 9MFY16 accounts have been prepared on 4.5% UFG benchmark due to pending approval by OGRA on court's stay.



Sui Southern Gas Company Limited

BALANCE SHEET

	30-Jun-15	30-Jun-14	30-Jun-13
	Annual	Annual	Annual
Non-Current Assets	74,429	70,401	67,999
Investments (Incl. associates)	1,282	1,136	1,095
Equity	1,282	1,136	1,095
Debt			
Current Assets	201,234	161,349	127,185
Inventory	1,043	1,068	803
Trade Receivables	116,150	99,643	93,444
Others	84,040	60,638	32,938
Total Assets	277,417	233,469	196,971
Debt	28,855	28,047	32,386
Short-term	989	3,141	4,018
Long-term (Incl. Current Maturity of long-term debt)	27,866	24,906	28,368
Other shortterm liabilities	207,249	159,936	117,904
Other Longterm Liabilities	22,485	21,619	20,547
Shareholder's Equity	18,827	23,867	26,135
Total Liabilities & Equity	277,417	233,469	196,971

INCOME STATEMENT

Turnover	162,583	153,284	151,638
Gross Profit	(7,982)	(8,968)	3,490
Other Income	5,553	9,088	2,236
Financial Charges	(2,607)	(2,490)	(2,054)
Net Income	(5,391)	(3,753)	248

Cashflow Statement

EBITDA	4,868	7,003	15,164
Free Cashflow from Operations (FCFO)	(866)	1,753	12,346
Net Cash changes in Working Capital	9,337	11,533	(12,790)
Net Cash from Operating Activities	5,686	10,565	(2,687)
Net Cash from Investing Activities	(6,708)	(5,865)	(6,915)
Net Cash from Financing Activities	806	(4,348)	8,947
Net Cash generated during the period	(216)	352	(655)

Ratio Analysis

Performance

Turnover Growth	6.1%	1.1%	15.8%
Gross Margin	-4.9%	-5.9%	2.3%
Net Margin	-3.3%	-2.4%	0.2%
ROE	-31.1%	-17.1%	0.9%

Coverages

Debt Service Coverage (x) (FCFO/Gross Interest+CMLTD+Uncovered STB)	0.0	0.2	2.1
Interest Coverage (x) (FCFO/Gross Interest)	-0.3	0.6	5.1
Debt Payback (Years) (Total Lt.Debt (excluding Covered Short Term Borrowings) / FCFC)	-9.1	-27.3	2.9

Liquidity

Net Cash Cycle (Inventory Days + Receivable Days - Payable Days)	-48	0	10
--	-----	---	----

Capital Structure (Total Debt/Total Debt+Equity)

	60.5%	54.0%	55.3%
--	-------	-------	-------



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		SHORT TERM RATINGS
AAA AA+ AA AA- A+ A A-	<p>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.</p> <p>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.</p> <p>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.</p>	<p>A1+: The highest capacity for timely repayment.</p> <p>A1: A strong capacity for timely repayment.</p> <p>A2: A satisfactory capacity for timely repayment. This may be susceptible to adverse changes in business, economic, or financial conditions.</p> <p>A3: An adequate capacity for timely repayment. Such capacity is susceptible to adverse changes in business, economic, or financial conditions.</p> <p>B: The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions.</p> <p>C: An inadequate capacity to ensure timely repayment.</p>
BBB+ BBB BBB-	<p>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.</p>	
BB+ BB BB-	<p>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.</p>	
B+ B B-	<p>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.</p>	
CCC CC C	<p>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.</p>	
D	<p>Obligations are currently in default.</p>	

<p>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.</p>	<p>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’.</p>	<p>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.</p>	<p>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.</p>
---	---	--	---

Disclaimer: PACRA's ratings are an assessment of the credit standing of entities/issues 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.



Rated Entity

Name of Rated Entity
Sector
Type of Relationship

Sui Southern Gas Company Limited
 Utilities
 Solicited

Purpose of the Rating

Independent Risk Assessment

Rating History

Dissemination Date	Long Term	Short Term	Outlook	Action
25-Jun-16	A+	A1	RW(-ve)	Downgrade
26-Jun-15	AA-	A1	RW (-ve)	Downgrade
26-Jun-14	AA-	A1+	RW(-ve)	Maintain
3-Jun-13	AA-	A1+	RW(-ve)	Maintain
28-Jan-13	AA-	A1+	RW(-ve)	Maintain
04-Apr-12	AA-	A1+	RW	Maintain
13-Apr-11	AA-	A1+	Negative	Maintain

Methodology:
Sector Research

Corporate Rating Methodology
 Gas Utilities - Viewpoint | May-16

Rating Analysts

Miqdad Haider miqdad.haider@pacra.com (92-42-35869504)	Saira Rizwan saira.rizwan@pacra.com (92-42-35869504)
---	--

Rating Team Statement

Rating Procedure

Rating is an opinion on relative credit worthiness of an entity or debt instrument. It does not constitute recommendation to buy, hold or sell any security. The rating team for this assignment does not have any beneficial interest, direct or indirect in the rated entity/instrument.

Disclaimer

Rating Shopping

PACRA maintains principle of integrity in seeking rating business. PACRA has used due care in preparation of this document. Our information has been obtained directly from the underlying entity and public sources we consider to be reliable but its accuracy or completeness is not guaranteed. PACRA shall owe no liability whatsoever to any loss or damage caused by or resulting from any error in such information.

Conflict of Interest

PACRA, 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 done by them.

The analysts involved in the rating process do not have any interest in a credit rating or any of its family members has any such interest

The analysts and members of the rating committees including the external member members have disclosed all the conflict of interest, including those of their family members, if any, to the Compliance Officer PACRA

The analysts or any of its family members do not buy or sell or engage in any transaction in any security which falls in the analyst's area of primary analytical responsibility. This is, however, not applicable on investment in securities through collective investment schemes. PACRA has established appropriate policies governing investments and trading in securities by its employees

PACRA may provide consultancy/advisory services or other services to any of its clients or to any of its clients' associated companies and associated undertakings that is being rated or has been rated by it. In such cases, PACRA has adequate mechanism in place ensuring that provision of such services does not lead to a conflict of interest situation with its rating activities

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 ii) fee mandate - signed with the payer, which can be different from the entity

PACRA ensures that the credit rating assigned to an entity or instrument should 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

Surveillance

PACRA monitors all the outstanding ratings continuously and any potential change therein due to any event associated with the rated entity/ issuer, the security

arrangement, the industry etc, is disseminated to the market, in a timely and effective manner, after appropriate consultation with the entity/issuer

PACRA reviews all the outstanding ratings on annual basis or as and when required by any stakeholder (including creditor) or upon the occurrence of such an event which requires to do so

PACRA initiates immediate review of the outstanding rating(s) upon becoming aware of any information that may be reasonable be expected to result in any change (including downgrade) in the rating

Reporting of Misconduct

PACRA has framed and implemented whistle-blower policy encouraging all employees to intimate the compliance officer any unethical practice or misconduct

relating to the credit rating by another employees of the company that came to his/her knowledge. The Compliance Officer reports to the BoD and SECP

Confidentiality

PACRA has framed a confidentiality policy to prevent abuse of the non-public information by its employees and other persons involved in the rating process, sharing and dissemination of the non-public information by such persons to outside parties

Where feasible and appropriate, prior to issuing or revising a rating, PACRA informs the issuer of the critical information and principal considerations upon which a rating will be based and provide the opportunity to clarify any likely factual misperception or other matter that PACRA would wish to be made aware of in order to produce a fair rating. PACRA duly evaluates the response. Where in a particular circumstance PACRA has not informed the entity/issuer prior to issuing or revising a rating, it informs the entity/issuer as soon as practical thereafter

Prohibition

None of the information in this document may be copied or otherwise reproduced, stored or disseminated in whole or in part in any form or by any means

whatsoever by any person without PACRA's written consent. PACRA reports and ratings constitute opinions, not recommendations to buy or to sell

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.