



## Today's Daily

### ■ Power: Debt clearance plan 'sugar-coats' arrears

News flows of a mechanism for re-profiling debt arrears in the power chain have pushed circular debt back to the limelight, where noteworthy developments include: 1) power sector arrears climbing to PkR472.7bn (PkR922bn including PkR450bn parked in Government Power Holdings Pvt Ltd) a rise of PkR79.7bn during CY17, 2) possible retirement of PkR514bn (with PkR140bn in the short run) in debt as of Dec'17 with a mix of commercial financing (for GPHL and DISCOs) and TFC's issued against payables due to IPPs (similar to circular debt resolution plan entered into by PSO in July'12 for PkR43.8bn at coupon of 11.5%) and 3) continuation of previously imposed surcharges being enacted through NEPRA, resulting in additional annual collections of PkR~59.05bn in FY18 with the majority of funds going towards rationalization surcharge to collect operational cost of DISCOs and tariff setting not covered in the tariff itself, varying across consumer categories and DISCOs. On all these fronts, we look at likely factors impacting the country's energy chain, where we believe a thorough, verified enactment of TFCs against receivables to IPPs is a given, largely re-profiling debt in the sector and formalizing arrears to IPPs, in our view. At the same time, formalization of debts due in the sector with additional liquidity from periodic coupon payments, and a FO-lite future make PSO a key beneficiary of this reform. At a June'18 TP of PkR382/sh current price levels offer 25% upside.

#### KSE100 - Index

Current	43,539.60
Previous	43,363.21
Chg.	0.41%

#### Mkt Cap. (PkRbn/US\$bn)

Current	9,063 / 81.97
Previous	9,065 / 81.98
Chg.	-0.02%

#### Daily Turnover (mn)

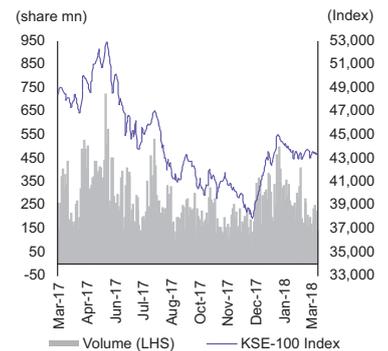
Current	115.97
Previous	193.40
Chg.	-40.0%

#### Value Traded (PkRmn/US\$m)

Current	5,259 / 47.56
Previous	6,700 / 60.59
Chg.	-21.5%

### News and Views

- The Adviser to PM on Finance, Miftah Ismail on Monday said that the GoP would announce a new amnesty scheme in a few days. In a related news, PSX officials meeting with Miftah Ismail ended on a positive note with the capital market's top echelons optimistic about the GoP's willingness to address the tax issues that impede the bourse's growth.
- Central Development Working Party (CDWP) has approved 34 projects worth PkR365.5bn out of which five projects valuing PkR333.18bn were referred to ECNEC for final approval. In this meeting, CDWP also referred the phase-I of the mega water reservoir Bhasha Dam with an estimated cost of PkR649bn for the approval of ECNEC.
- FPCCI advised the GoP to consider exempting export-oriented sectors from all the taxes in the upcoming five-year trade policy framework. FPCCI submitted its set of recommendations for the proposed strategic trade policy framework (2018-2023), which would soon be announced by the commerce ministry.



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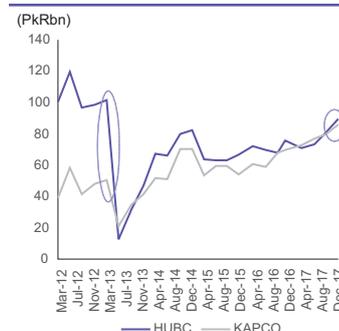
## Power: Debt clearance plan 'sugar-coats' arrears

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**Consistent late payment collections for PSO:** For the nation's power chain, these developments could bode well, particularly for the cash strapped state OMC, PSO. While no mention of the OMC's sizeable arrears (PkR205.5bn from power sector rising PkR29.3bn FYTD i.e average addition of 3.7bn/month) has been made in the current plan, any clearance of EPP payments (energy purchase price of which fuel cost is the largest component) would add liquidity by streamlining penal payments to the OMC, compensated through any coupon payments for TFCs issued to IPPs.

**Minor relief for stretched IPP balance sheets:** Overdue receivables of both HUBC and KAPCO almost peaked in 9MFY13 at PkR101.8bn and PkR50.3bn, respectively. Despite adverse liquidity situation, both the companies continued with high payout ratios (HUBC: 91.7%, KAPCO: 89.8%) on the back of short term borrowings. While the number stands at PkR89.8/PkR85.9bn for HUBC/KAPCO as of Dec'17, our estimates suggest that dividend yields of HUBC/KAPCO for the next 4Qs stand at 7.7%/15%. To highlight, the settlement of circular debt would have minimal earnings impact as surplus mark-up differential between receivables and payables is set aside by interest on short term borrowings. Moreover, for

Overdue Receivables Outstanding



Source: Company Report & AKD Research

Major Receivables Outstanding (in PkR BN) for PSO

	Dec'17	Jul'17	Jul'16
Power Sector	203.1	176.1	146.5
LNG (SNGPL)	16.5	14	11
Price Differential From GoP	9.6	9.6	9.6
PIA	13.3	13.3	12.3
Sum	242.5	213.0	179.4
Late Payment Surcharge	80.5	73.7	62.3
Total + LPS	323	286.7	241.7

Source: Co. Reports & AKD Research

Tariff & Non-tariff surcharges

Tariff Rationalisation (non-tariff built into monthly, category-wise surcharge)	1.54
Neelum Jhelum Surcharge	0.10
Debt Servicing surcharge	0.43

Source: IMF, GoP, AKD Research



HUBC, additional liquidity would aid in the investment theme it is pursuing with regards to TEL (required Financial Close on Mar 9'18) and SECMC specifically.

**Outlook:** Refraining from drawing parallels to past clearance payments (June'2012 and June'2013) we believe a thorough, verified enactment of TFCs against receivables to IPPs is a given, largely re-profiling debt in the sector and formalizing arrears to IPPs, in our view. This would in effect add additional cover to government backed loans, guaranteeing payments due under Power Purchase Agreements, while providing room to the GoP for payments to be made to planned generation additions to come online over the medium term. Furthermore, additional income on TFCs, and whether penal income payments on outstanding receivables vs. late payment surcharges to PSO are compensated for by the coupon rate on said TFCs (current issue 5yr PIBs yield 8.41%) are going to remain major areas of concern for IPPs.

**Investment Perspective:** PSO remains stuck with its stock of receivables, where receipt of late payment surcharge from IPPs should be compensated through any coupon payments accompanying TFCs, while the OMC would have to hold off on clearing the entire stock of receivables from the power space till the TFCs mature. At the same time, formalization of debts due in the sector with additional liquidity from periodic coupon payments, and a FO-lite future make PSO a key beneficiary of this reform. At a June'18 TP of PKR382/sh current price levels offer 25% upside where possible regularization of overdue payments (accompanying penal income) from the power sector, re-affirms our BUY call



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Accumulate	> 5% to < 20% upside potential
Neutral	≤ 5% to ≥ -5% potential
Reduce	< -5% to > -20% downside potential
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