# K-Electric Limited Investor Presentation

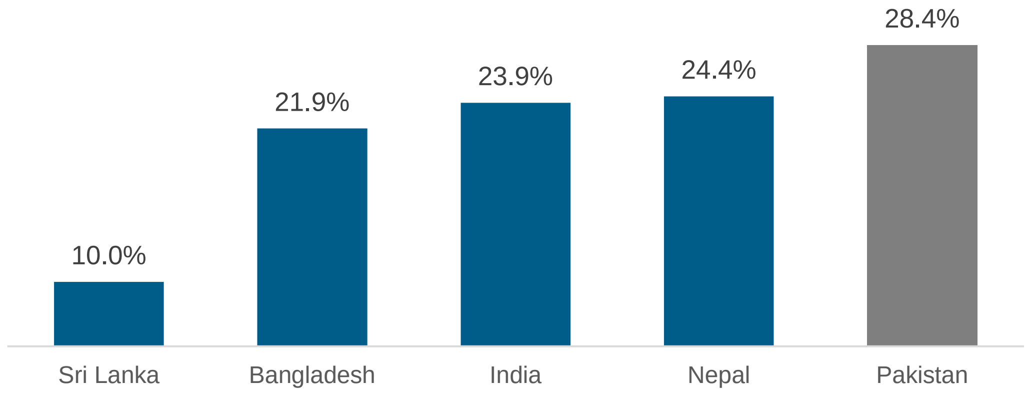
November 2019

# Pakistan Power Sector – State of the Industry

**Despite capacity additions of over 10,000 MW of power generation in the last 5 years, overall energy planning remained fragmented across the energy value chain, with little focus on improving the energy mix and upgrading Transmission and Distribution capacity**

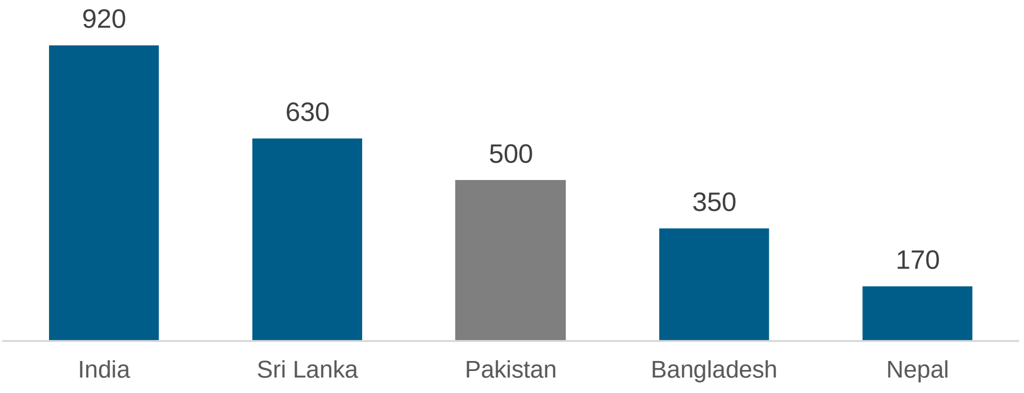
## AT&C Loss Comparison

***Highest AT&C Losses in the region* – need for technological and process improvements**



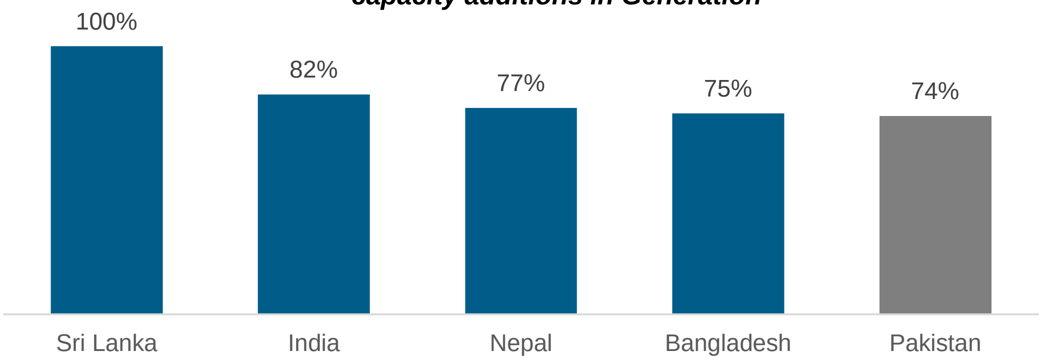

## Per Capita Consumption (kWh)

***Low per capita consumption – potential for future growth through investments in T&D business***




## Electrification Rate

***26% of the country's population does not have access to grid electricity* – signaling lack of investment in T&D segment, despite capacity additions in Generation**




## Need for continued investments

Potential for **USD 80 Billion of future investments** to bring operational improvements along with sector reforms – out of these **at least 50% are required in Transmission and Distribution upgrades**

> *"… Pakistani power sector including generation, transmission and up-gradation has over USD 80 Billion investment opportunities and foreign direct investment was pouring as multiple companies have shown their interest to invest"*
>
> ***Omar Ayub, Minister for Energy, Government of Pakistan***

Source: NEPRA State of Industry Report, Power Division Pakistan, World Bank, Ministry of Power & Renewable Energy (Srilanka), Institute of Energy Economics, Nepal Electricity Authority, International Energy Agency (IEA), News Reports

# Strategic Importance of Karachi

**The city of Karachi is essential to Pakistan's economy and drives much of the country's economic growth. As the city's sole electricity provider, KE is of strategic importance to the municipality and the country**

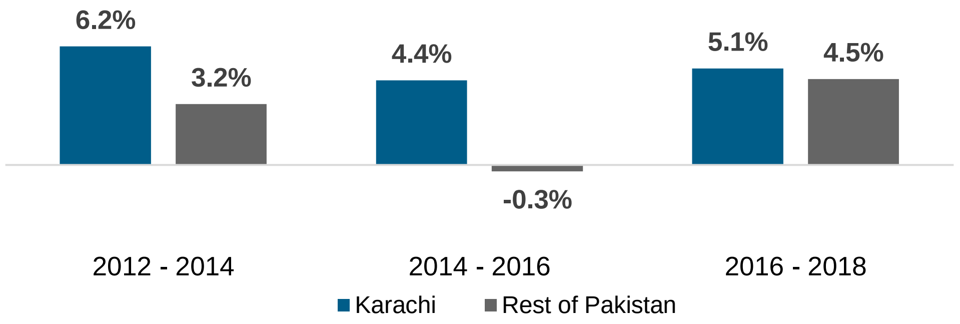
## Karachi's Importance to Pakistan

- Karachi is the commercial hub and gateway of Pakistan – accounts for c. 20% of the country's GDP
- Home to Pakistan Stock Exchange, making it the financial centre of Pakistan
- c. 40% of large-scale manufacturing employment is in Karachi
- Population is expected to grow at a CAGR of c. 2.5% in the next 5 years
- Following government initiatives among others would lead to further increase in industrial and commercial activity, resulting in increased power demand
  - Setting up of Special Economic Zone (SEZ) in Dhabeji region
  - Development of National Industrial Park near Port Qasim, Karachi

## Rest of Pakistan vs. Karachi – Growth in Peak Demand[1] (MW)

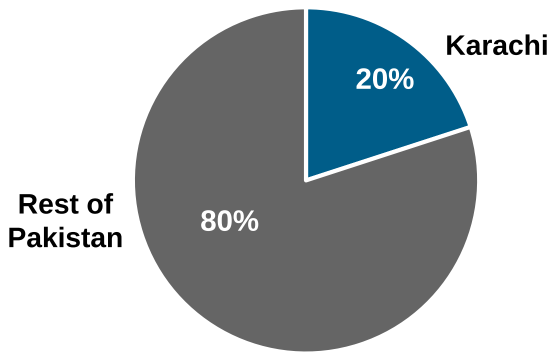
***Growth in power demand in Karachi has remained higher than rest of the country***

| Growth in Peak Demand CAGR ( FY 12 – 18) | |
|---|---|
| **Karachi** | **5.2%** |
| **Rest of Pakistan** | **2.4%** |

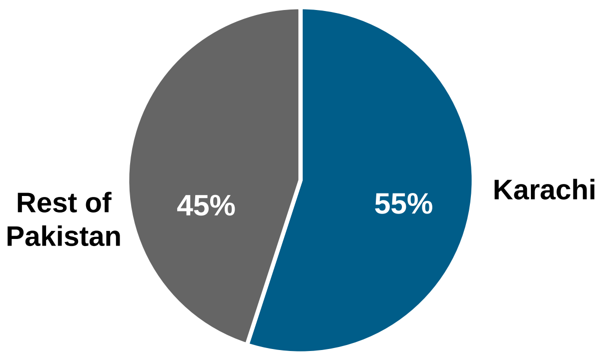



## Karachi's Contribution to Pakistan's Economy

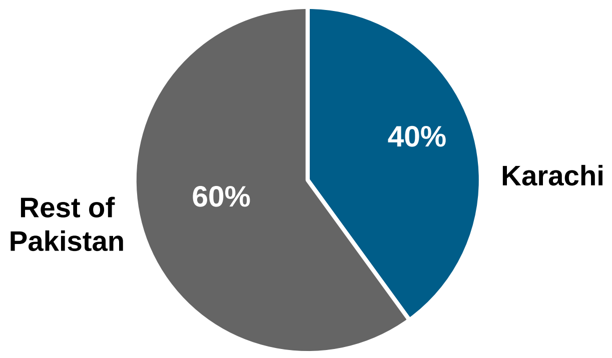
**Gross Domestic Product**




**Tax Revenue**




**Large-scale Manufacturing Employment**




Source: Asian Development Bank & United Nations population estimates and projections of major Urban Agglomerations, World Bank, News Reports, NEPRA State of Industry Report

1. Peak demand for PEPCO area in 2019 is not available

# Pakistan Power Sector – Reforms Underway

**Policy reforms are underway to address key power sector issues including circular debt and other structural weaknesses – improvement of ecosystem and system performance will definitely fuel economic growth led by domestic and export-led businesses**

## Challenges

- **Circular Debt**
- **Significant increase in Capacity Payments**
- **Tariff Subsidies**
- **High Losses & Need for Technological Upgrade**
- **Weak Governance of ex-WAPDA Entities**

## Measures

### Sustainable Capacity

- Shift to low cost sources (coal, hydel, renewables, etc)
- Targeted fuel mix by 2040: Hydel (40%), Renewables (16%) and Local Coal (25%)
- Attract investment in on-grid and off-grid renewables for greater access
- Integrated planning to improve demand forecasting which will help avoid capacity payments for idle capacity

### Structural Changes

- Planned privatization of state-owned distribution companies
- Regulatory changes including action against power theft
- Gradual phasing out of subsidies through increase in consumer-end tariff
- Competitive bidding
- Opening up of markets allowing wider access to distribution companies

### Efficiency Improvements

- Introduction of technology (Aerial Bundled Cabling, Smart Meters, etc)
- Minimize losses through upgrading T&D network and improve recovery

## Positive Outlook

- **GoP's target to erase circular debt by end of 2020**
- **Addition of low-cost generation**
- **Privatization of state-owned DISCOs**
- **Improved Operational Efficiency, Greater Transparency and Accountability**
- **Reduction in power outages and improved service levels**

Source: World Economic Forum, News Reports

# Business Overview

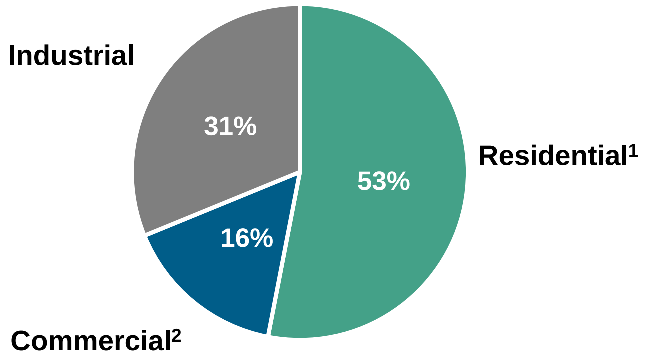
**As the only vertically integrated power supply company in Pakistan, KE has a robust network to ensure sustainable and reliable power supply to Karachi and its adjoining areas**

## Presence Across the Entire Power Value Chain

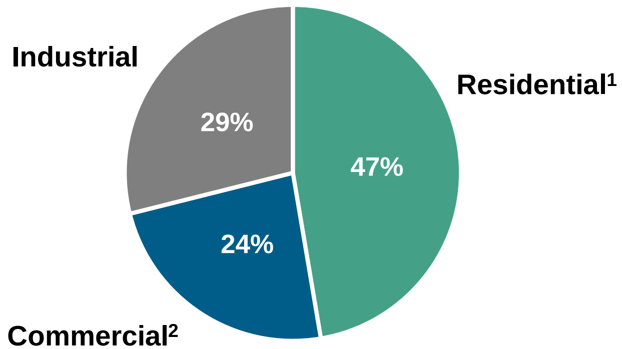
| Generation | Transmission | Distribution |
|---|---|---|
| Own Generation<br>Power Purchases | Grid Stations | End User |
| **5 plants** with installed capacity of **2,267 MW** and 1,300+ MW of arrangement with external sources | **6,078 MVAs** transmission capacity through **68 grid stations**, **160 Power Trafos** & over **1,283 km of EHT lines** | **7,702 MVAs** distribution capacity through **1,807 feeders** & **28,000+ PMTs and substations** |

## A Diversified Customer Base

**Customer Breakdown (Units Billed)**

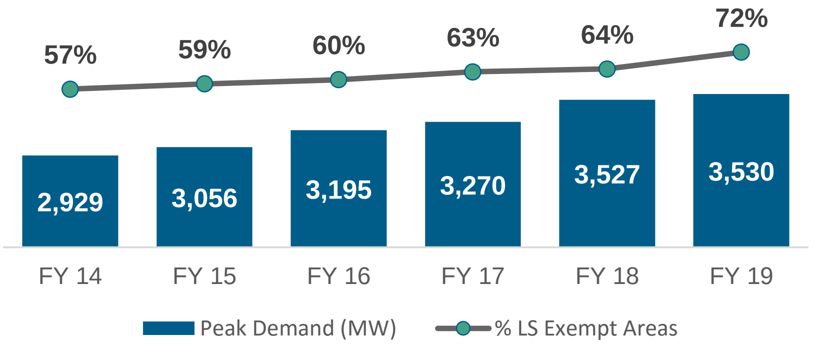



**Customer Breakdown (Amount Billed)**




## Growing Power Demand and Reduction in Load-shed

***Capacity additions, loss reduction initiatives and process improvements have enabled KE to exempt over 70% of the service territory from load-shed***




1. Residential includes Domestic, Agriculture, Street light and General Services
2. Commercial includes Bulk Supply consumers

Note: Public sector consumers account for c. 9% of annual units billed

# Brief History & Overview

**Incorporated in 1913, KE is the only power utility company having presence across the entire energy value chain, and has a customer base of more than 2.8 Million**

## From KESC to KE[1]

| | |
|---|---|
| 1913 | KESC Incorporated |
| 1949 | 1st Company to list on KSE |
| 1952 | Nationalization of KESC |
| 2005 | Privatization |
| 2009 | Turnaround Commences |
| 2012 | Profits after 17 years |
| 2019 | Continued Focus on Sustainability & Growth |

### KE in 2009

| | | |
|---|---|---|
| USD 1,084 Million<br>FY09 Revenue | USD (87) Million<br>FY09 EBITDA | 1,685 MW<br>Generation Capacity |
| 35.9%<br>T&D losses | c. 2.0 Million<br>Customers | 52<br>Grid Stations |

Severe lack of Investment and old & dilapidated Infrastructure resulting in frequent outages and unannounced load-shed

Cash Burn of USD (180) Million in FY 09

### KE in 2019[2]

| | | |
|---|---|---|
| USD 1,975 Million<br>FY 18 Revenue | USD 295 Million<br>FY 18 EBITDA | 2,267 MW<br>Generation Capacity |
| 19.1%<br>T&D losses | > 2.8 Million<br>Customers | 68<br>Grid Stations |

Over USD 2.4 Billion invested across the value chain since 2009

Profitable after 17 years in FY 12 – *IFC and ADB converted their long-term financing of USD 50Mn into equity*

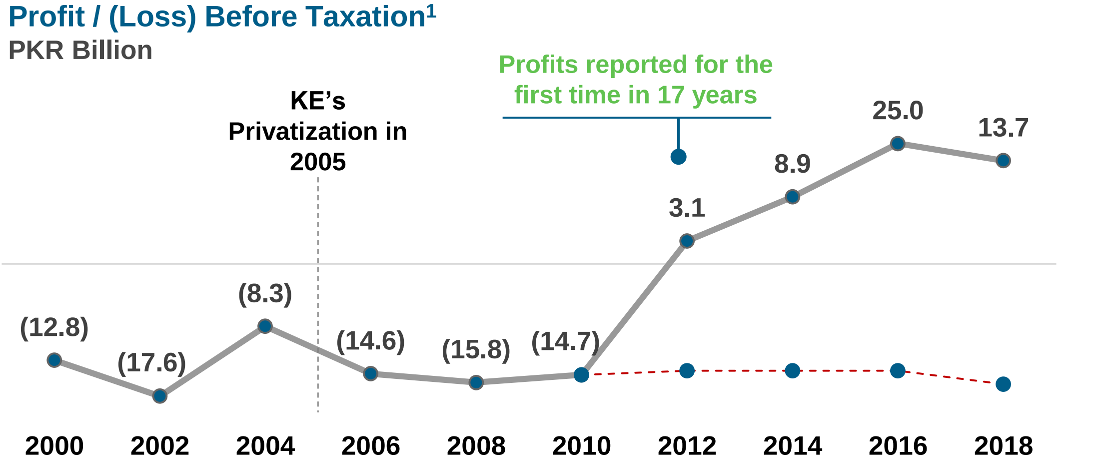
1. Rebranded to KE in 2014

2. KE's financials for FY 19 are in the process of finalization

# KE's Turnaround – A Success Story

**Privatized in 2005, KE's turnaround success presents a classic example of targeted and well-timed investments transforming a cash-bleed, loss making entity into a profit-making utility driven by significant investments and operational improvements**

## KE's Turnaround from a troubled loss-making entity

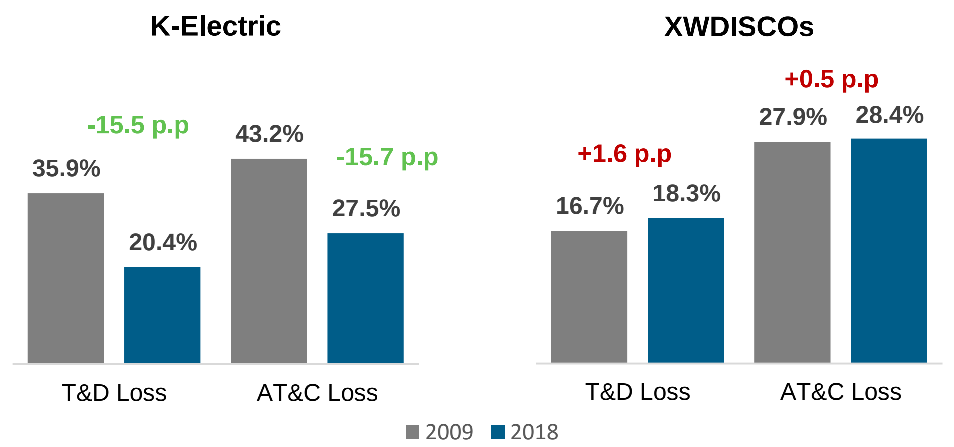



**KE's Privatization & Turnaround – Setting a precedent for the Power Sector**

- To keep KE's operations afloat, **annual average operational subsidy of c. PKR 9.5 Billion** had to be provided by GoP during FY 2003 to FY 2005, which was not required post privatization – losses borne by KE's private investors
- **Evident from the performance of XWDISCOs**, had KE not been privatized, the company would have continued on a loss-making trajectory, **burdening the GoP in the form of operational subsidy – KE's improvement in AT&C losses of 15.7% points (Annual impact of c. PKR 50 Billion[2])**
- XWDISCOs reported a cumulative loss of **c. PKR 207 Billion** from 2013 to 2016 – **Eight out of ten state-owned distribution companies reported losses in FY 16** and are heavily dependent upon GoP support

## Operational Improvements outperforming state-owned DISCOs

***Significant Loss Reduction by KE, whereas losses of XWDISCOs have increased***




- In view of the above significant improvements shown by KE post privatization, **NEPRA has also recommended the GoP to consider privatization of XWDISCOs, encouraging private investments**
- This would **improve the governance and efficiency of XWDISCOs**, make them **financially self-sufficient**, thus **reduce the burden on national exchequer and enable the sector to be financially sustainable**

Source: State Bank of Pakistan, NEPRA State of Industry Report
1. Excluding operational subsidy provided by GoP
2. Computed as (FY 19 sentout x 15.7% x Average Tariff of PKR 18.2/kWh)

# Operational Performance since 2009

**Through investments of over USD 2.4 Billion across the value chain during FY 09 to FY 19[1], KE's management focused on enhancing fleet efficiency, reducing T&D losses and improving operational processes to unlock value**

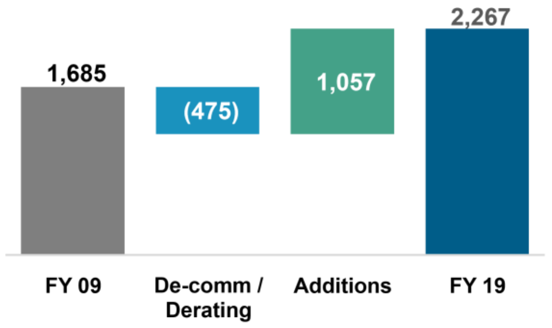
## Investments across the value chain since 2009

### GENERATION

**c. USD 1,090 MILLION[1]**

- Induction of **4 modern and highly efficient generation plants**
- **Addition of 1,057 MW** of generation capacity
- **Fleet efficiency** improved from **30% in FY 09 to 37% in FY 19**

**Capacity Addition (MW)**




### TRANSMISSION

**c. USD 620 MILLION[1]**

- Focus on transmission capacity additions and infrastructure rehabilitation
- Addition of **16 new grid stations**
- **Transmission capacity enhanced by 42%**
- **c. 404 km of old circuit length rehabilitated** and over **98 km of EHT lines** added
- Significant reduction in transmission loss – 2.8% points from over 4% in 2008 to 1.2% in FY 19
- **64% reduction** in trafo / grid equipment tripping

### DISTRIBUTION

**c. USD 700 MILLION[1]**

- **Reduction in T&D losses by 16.8% points**
- **Capacity enhancement by over 3,000 MVAs (c. 64%)**
- **7,500+ PMTs** have been **converted onto Aerial Bundled Cabling** (ABC)
- Setting up of Integrated Business Centers – a one-stop solution for customers
- Focus on customer centricity – getting closer to customers through Call-Centres and e-solutions
- Process improvements including implementation of SAP-ISU billing

**>70%**
of Karachi load-shed free vs. 23% in 2009

**100%**
Industrial zone load-shed exemption

**19.1%**
T&D losses – improvement of 16.8% points since 2009

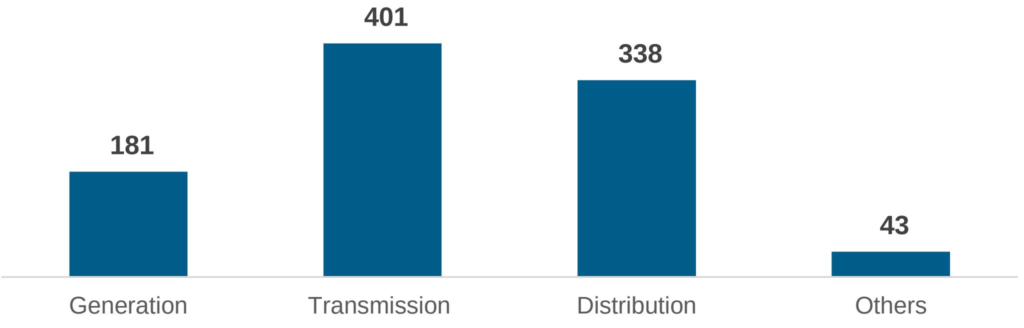
1. Includes Capex numbers for FY 19 which are provisional and unaudited

# Investments made Across the Value Chain in Last 3 Years

**Over the last three years, various initiatives were taken across the energy value chain to enhance capacity, improve reliability of the network along with targeted loss reduction**

## Capex FY 17 – FY 19[1] (USD Million)

***Over USD 960 Million invested across the value chain in the last 3 years***



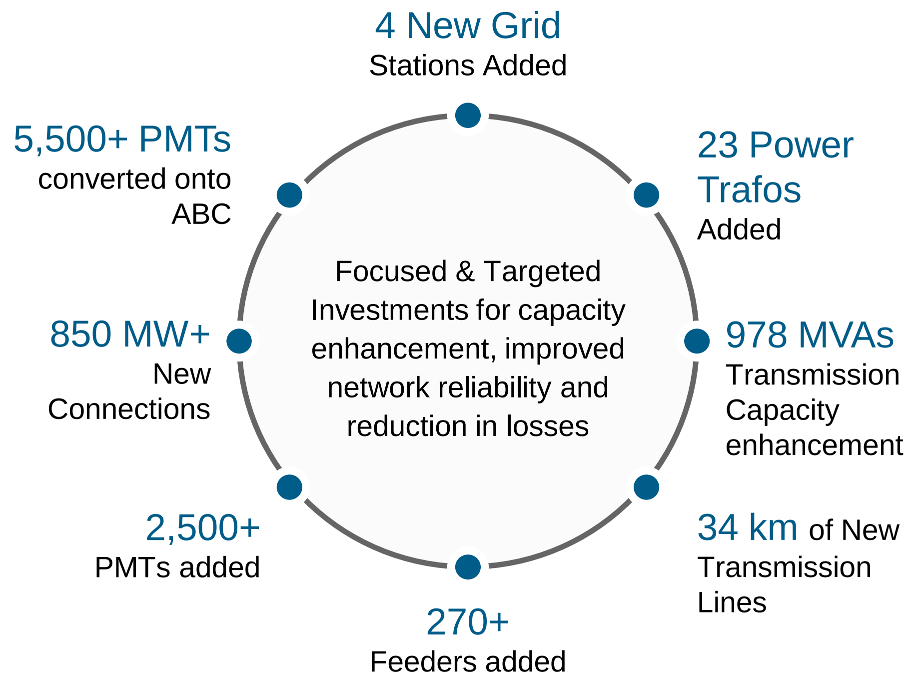

## Operational Improvements

- Overhaul and rehabilitation works resulted in **increase in average Gross Dependable Capacity (GDC) by c. 70 MW** as compared to FY 16
- Significant progress was made on KE's **over USD 450 Million TP – 1000** project to overcome transmission constraints and facilitate sent-out growth
- **T&D losses reduced by over 3% points** from FY 16 levels along with **c. 4% points improvement in overall recovery levels**
- **Recovery drives / campaigns** to engage defaulters such as *'Current Bill ka Waada'*
- **Technological advancements** including AMI Infrastructure, launch of KE Live App

## Capacity Addition & System Improvements in last 3 years

**Power Supply added to KE's System in last 3 Years**

| National Grid | Oursun | SNPC | FPCL |
|---|---|---|---|
| **(150 MW)** | **(50 MW)** | **(101 MW)** | **(52 MW)** |
| June, 2019 | Nov, 2018 | Jan, 2018 | May, 2017 |

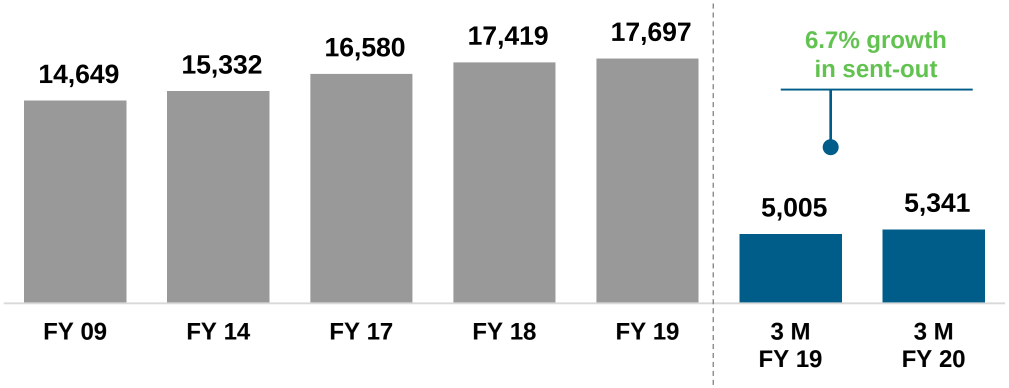



1. Capex numbers for FY 19 are provisional and unaudited

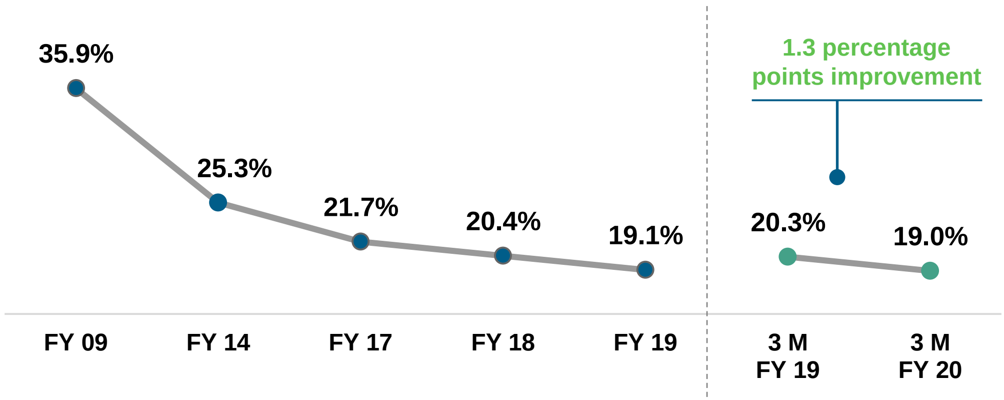
# Operational Performance – Generation, Transmission & Distribution

**Driven by focused investments, the company has continued to improve on the operational parameters – strong operational performance in the first quarter of FY 20 to further the operational improvements of previous years**

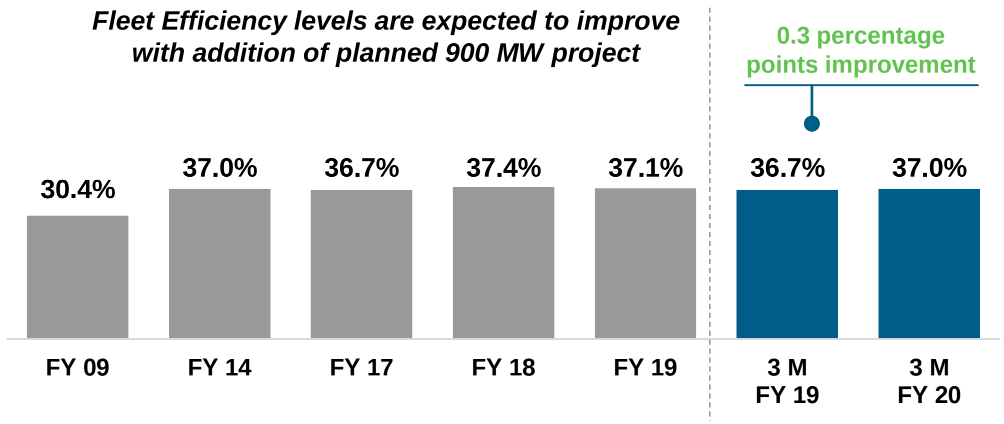
## Sent-out (GWh)



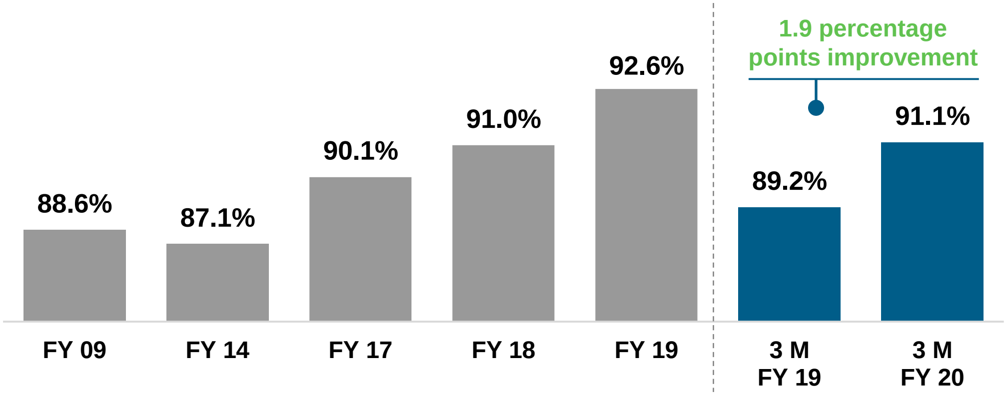

## Rolling Average T&D Losses (%)




## Generation Fleet Efficiency (%)




## Recovery Ratio (%)




1. FY 19 and 3M FY 20 numbers are provisional and unaudited

# Financial Performance

**Despite change in tariff, the company continued to perform on the operational front which translated into improved financial performance in FY 18**

## Financial Highlights

### Change in Tariff Level & Structure

- Change in tariff structure and levels impacted FY 17 profitability as compared to FY 16
- KE expects a positive outcome to its Appellate Tribunal case on key MYT issues

### Continuous Investments and Improved Operational Performance in FY 18

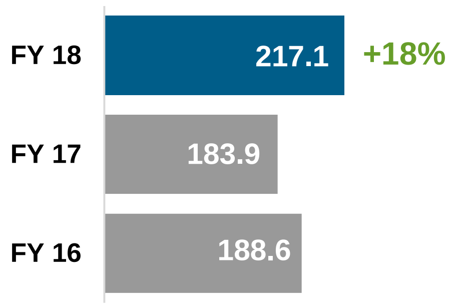
- Driven by operational improvements including sent-out and T&D losses, FY 18 marked improvements in financial performance as compared to FY 17

### Sustained Financial Outlook

- Continued and sustained operational improvements in future through investments in all core functions will translate into improved financial results

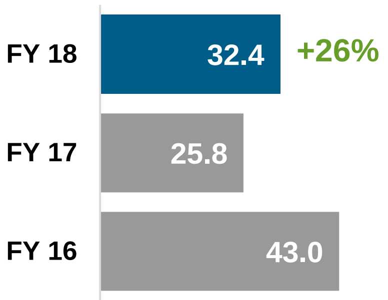
### Revenue

PKR Billion



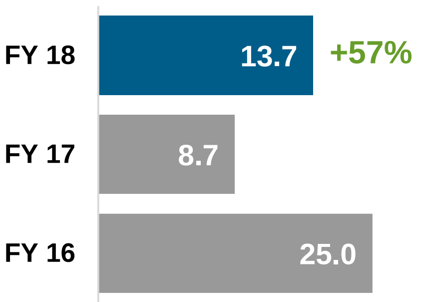

### EBITDA

PKR Billion



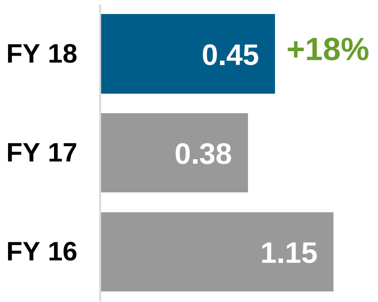

### Profit Before Taxation

PKR Billion



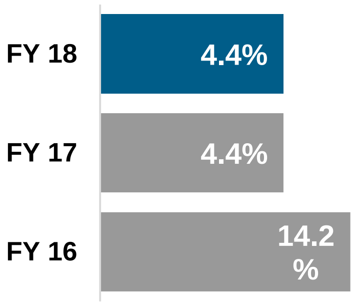

### Earnings Per Share

PKR



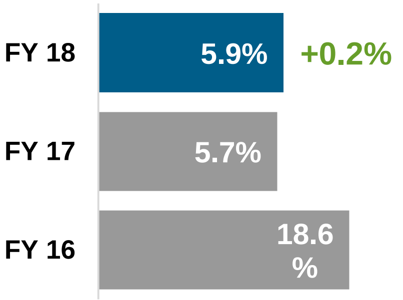

### Return on PPE[1]

%




### Return on Equity[2]

%




Note: PPE – Property, Plant and Equipment
1. RoPPE adjusted for surplus and incremental depreciation (FY 18: 9.1%, FY 17: 9.8%)
2. RoE adjusted for surplus and incremental depreciation (FY 18: 12.1% , FY 17: 12.2%)

# Key Financing Initiatives

**Investors have shown continued trust and confidence in the company's fundamentals, enabling KE to make the planned investments on accelerated basis and further the positive trajectory of operational improvements**

## Key Financing Initiatives


***Issuance of PKR 10 Billion Islamic Commercial Paper*** *– Pakistan's largest privately placed Shariah-compliant Islamic Commercial Paper*

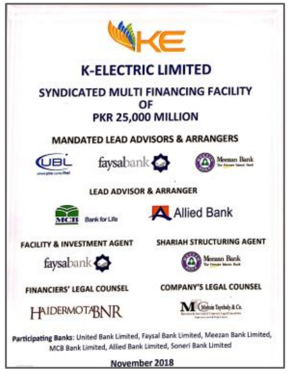

***USD 50 Million funding arranged from Guarantco.*** *for projects in Generation, Transmission and Distribution – will enable KE to capitalize upon the growth potential*

**VIS** Credit Rating Company Limited

*"VIS Credit Rating Company Limited (VIS) has assigned preliminary rating of AA+ (Double A Plus) to K-Electric Limited's (KE) proposed Rs. 25 billion Sukuk. KE's long-term entity and Sukuk rating (Rs. 22b Sukuk) have been reaffirmed at AA (Double A) and AA+ (Double A Plus), respectively. The Company's short-term ratings have been upgraded from A-1 (Single A One) to 'A-1+' (Sindh A-One Plus)….Rating assigned to KE's outstanding Islamic Commercial Paper (ICP-A) has also been upgraded to 'A-1+' (A-One Plus)"*

***Press Release, VIS Credit Rating Company Limited, October 14, 2019***

***Improved Credit Rating*** *following notification of KE's MYT and on the back of improved operational and financial outlook of the company*




***Syndicate Financing of PKR 25 Billion*** *Besides TP – 1000 project, the proceeds of this loan are also being utilized to fund ongoing Distribution projects*

# Determined MYT

**As compared to KE's Previous MYT, the Determined MYT presents a different, de-risked, Return on RAB structure with additional upsides for KE to unlock value and further its improvement trajectory**

## Opportunities to Unlock Value under the Determined MYT

As highlighted below, the Determined MYT presents several upsides for KE to capitalize upon. KE also remains confident of a positive outcome to its Appellate Tribunal case on key MYT issues including application of notional Debt to Equity ratio by NEPRA while calculating the allowed returns

**Return on RAB structure** – allows for a long-term, de-risked construct since KE's RAB will continue to increase as key projects come online and the structure is inline with other power sector entities

**Dollarized returns** across the value chain have been allowed

**Operational Efficiencies –** outperforming NEPRA benchmarks for T&D loss, sent-out growth and beating NEPRA projected O&M costs

**Removal of "-X" Factor from O&M Indexation for Generation** – similar to IPPs

**Allowance of Actual write-offs –** improved recovery which combined with allowed write-offs will minimize KE's recovery gap

**Mid-Term Review Mechanism in Tariff –** to re-assess certain assumptions including investments, exchange rates and working capital

**Investment Flexibility** – investments in new generation projects *(other than BQPS – III)*, subject to NEPRA's approval

**Tax / WWF / WPPF** allowed as pass-through items

**There are numerous opportunities to unlock value under the long-term de-risked return on RAB structure while retaining KE's integrated nature of operations**

# Initiatives across the Energy Value Chain

**Targeted investments of c. USD 3 Billion in all core functions in the next four years would enable KE to unlock key value drivers under the MYT along with benefitting consumers and the economy at large**

## Investments across the Value Chain

### Generation

- Capacity addition of **c. 3,000 MW** – key projects include:
  - **900 MW** RLNG Plant – the project would significantly improve KE's overall fleet efficiency
  - **700 MW** Coal IPP (equity project)
  - c. 1,000 MW through external IPPs including 300 MW of renewables
- Planned projects would also diversify KE's fuel mix

### Transmission

- Capacity enhancement and improved network reliability through two key projects:
- TP – 1000: **addition of 1,000 MVAs**
  - 4 grid stations and 22 power trafos have been added under TP – 1000 project
- TP – 2: to further improve system / network reliability and facilitate sent-out growth

### Distribution

- Capacity enhancement through addition of **300 feeders** and **over 5,000 transformers**
- Conversion of **15,000 PMTs** onto ABC by 2023 – **significant reduction in losses**
- Targeted recovery drives / campaigns to engage defaulting consumers and **improve recovery levels**
- Simplified New Connection process – expected to add over 1,400 MW of new connections in the next four years
- Safety enhancement initiatives

**Investments of USD 3 Billion in the next four years to capitalize upon growth potential and provide consumer value**

- **Improved Network Reliability**
- **Reduction in Load-shed**
- **Process Automation and Improved Service Levels**
- **Enhanced Network Safety**
- **Industrial Connections fueling economic growth**

# Potential for Further Value Improvement through a Strategic Investor

**In addition to KE's robust investment plan of c. USD 3 Billion across the energy value chain, an aggressive, strategic investor, Capex plan would further improve Karachi's power infrastructure**

## Strategic Investment – Potential Impact

- An aggressive investment plan, would be an opportunity for Karachi's power sector to reach new levels of excellence – **would further allow KE to remain committed to ensure safe, reliable and uninterrupted supply of power for the citizens of Karachi through:**
  - Capacity additions across the power value chain
  - Reduced load-shed
  - Improved network reliability
  - Provision of N – 1 supply for low loss, strategic and industrial consumers
- Shanghai Electric Power (SEP) signed a Definitive Agreement to acquire 66.4% stake in the company in October 2016, subject to receipt of government and regulatory approvals and has presented such a plan to the GoP
- SEP is one of the largest electric power companies in Shanghai and is committed to developing the power sector worldwide through operations in over 20 countries outside of China
- SEP is a subsidiary of the State Power Investment Corporation of China (SPIC), one of China's big 4 generation companies with installed capacity of over 142,700 MW and also has operations in over 43 countries globally
- SPIC is an active participant in the development of Pakistan's power sector and is a key CPEC investor involved in a wide variety of projects

> *"… SEP will leverage its own strengths as a strategic investor and further realise K-Electric's potential to provide better services to the people of Pakistan and the Government of Pakistan."*
>
> ***Wang Yundan, Chairman SEP***

**An aggressive investment plan along with KE's planned initiatives would result in greater positive impact for KE's customers and Karachi, while also facilitating economic growth in Karachi and Pakistan**

# Key Challenges – Receivables from Government Entities and Departments

**Delays in release of payments from relevant authorities and growing receivables from government entities impacts the working capital position of the company for which continuous engagement with relevant stakeholders is being done**

## Receivables & Payables – Government Entities / Departments

| Receivables from Government Entities | PKR Billion |
|---|---|
| Tariff Differential Claims[1] | 149 |
| KWSB *"Strategic Customer"* | 32 |
| Government of Sindh (GoS) | 19 |
| Other Federal & Provincial Entities | 14 |
| **Total Receivables** | **214** |

–

| Payables to Government Entities | PKR Billion |
|---|---|
| NTDC / CPPA – G | 97 |
| SSGC | 14 |
| Other Federal & Provincial Entities | 6 |
| **Total Payables** | **117** |

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**Net Receivable to KE**

**c. PKR 98 Billion**

## KE seeks a fair and equitable resolution to the issue of receivables and payables

- KE is in continuous engagement with relevant stakeholders for a fair and expedient resolution to the issue of receivables and payables, including any mark-up
- Delays in release of TDC and energy dues of strategic customers including KWSB by GoP resulted in consequential delays in payments to NTDC / CPPA – G and SSGC
- Monthly payments are being received against KWSB dues since January 2016. Further, execution of a Power Supply Agreement with GoS guarantee around KWSB dues is in advanced stages
- Power Purchase Agreement with NTDC provides for a set-off mechanism through which KE's payables to NTDC / CPPA – G are to be off-set with TDC receivables – KE has net TDC receivables of c. PKR 52 Billion from the GoP
- GoP is considering revision in consumer-end tariff which would reduce accumulation in subsidy claims
- On the disputed mark-up, GoP is a party on both sides (receivables & payables) – establishes mutuality of obligations and accordingly, settlement of outstanding dues, including any mark-up, shall be done on net basis

1. Includes pending tariff variations

# Other Challenges

**The management is confident of the strategies put in place to mitigate other key challenges as highlighted below**

| Challenges | Description | Mitigating Strategy |
|---|---|---|
| **Demand-Supply Gap** | • Delayed finalization of MYT has resulted in consequential delays in execution of planned generation projects | • Planned 900 MW and 700 MW projects being pursued on fast track basis<br>• Engagement with GoP for additional supply from the National Grid to manage the growing power demand |
| **City Infrastructure and External Factors impacting Provision of Safe Power Supply** | • Encroachments and illegal settlements hinders access to certain areas<br>• Theft of earthing / grounding equipment<br>• Tampering with KE's network by TV cable / internet cable operators poses a safety hazard<br>• Right of Way ("RoW") impact timely execution of projects | • Continuous engagement with local administration / authorities on kunda removal drives / tampering with network / Right of Way issues<br>• Revalidation of grounding / earthing of HT / LT poles and change in specification of earthing / grounding material to avoid theft |
| **Consistency in Government / Regulatory Policies** | • Consistency in regulatory landscape and government policies to ensure that interest of all stakeholders is balanced | • Engagement at Government level and with the regulator to ensure certainty in regulatory and policy matters, enabling a pro-investment environment |

# The Journey Continues

**Capitalizing on the ongoing projects and with the continued investments, KE would continue to strive, improving the lives of people of Karachi and bringing economic prosperity in the country**

## Potential Impact

**Capacity Additions**

- Swift capacity additions and ability to provide new connections, particularly to industrial consumers on the back of increased T&D capacity

**Growth & Productivity**

- Operational improvements to translate into greater economic activity and industrial growth – direct impact on national GDP

**Operational Efficiency**

- System reliability and process improvements
- Reduced load-shed

**Socio-Economic Improvements**

- Reliability and sustainability in power supply to have a direct impact on Human Development Index

**Dollarized Returns**

- Accelerated Capex and dollarized returns across the value chain

**Enhanced Safety**

- Public Accident Prevention Plan focusing on pole grounding – enhancing overall safety levels

**Aligned with the mission of brightening lives by building the capacity to deliver uninterrupted, safe and affordable power to Karachiites, KE will continue to make investments across the value chain, enabling the Company to improve operationally whilst progressing on the value creation curve through innovation and technological advancements**

# Thank You

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