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Research Update:

Oman Power and Water Procurement Co. SAOC Downgraded To 'BBB+' Following Sovereign Downgrade; Outlook Negative

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Table Of Contents

Overview

Rating Action

Rationale

Outlook

Ratings Score Snapshot

Related Criteria And Research

Ratings List

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Overview

- On Nov. 20, 2015, we lowered our long-term sovereign credit ratings on the Sultanate of Oman to 'BBB+' from 'A-' and assigned a negative outlook.
- We align the rating and outlook on Oman Power and Water Procurement Co. SAOC (OPWP) with the rating and outlook on the sovereign, as per our criteria.
- As a result, we are lowering our rating on OPWP to 'BBB+' from 'A-'.
- The negative outlook on OPWP parallels our negative outlook on Oman.

Rating Action

On Nov. 25, 2015, Standard & Poor's Ratings Services lowered its long-term corporate credit rating on Oman Power and Water Procurement Co. SAOC (OPWP) to 'BBB+' from 'A-'. The outlook is negative.

Rationale

The downgrade follows a similar rating action on the Sultanate of Oman (see "The Sultanate of Oman Long-Term Rating Lowered To 'BBB+'; Outlook Negative; Short-Term Rating Affirmed At 'A-2'," published Nov. 20, 2015, on RatingsDirect).

We align the rating and outlook on OPWP with the rating and outlook on the sovereign. This reflects our opinion that there is an almost certain likelihood that the government of Oman would provide timely and sufficient extraordinary support to OPWP in the event of financial distress.

In accordance with our criteria for government-related entities (GREs), our rating approach is based on our view of OPWP's:

- Critical role as the monopoly buyer and supplier of bulk electricity and desalinated water in Oman. The government set up OPWP in 2005 as an intermediary between electricity producers and distributors. Its legal role is to secure the production capacity and output to meet "all reasonable demands" for electricity and to secure the production of desalinated water. This includes the critical function of forecasting Oman's demand and supply of electricity and related water over a seven-year period.
- Integral link with the Omani government, given the company's public

policy role and 100% state ownership through the Ministry of Finance and government-owned Electricity Holding Co. SAOC (EHC). The government created OPWP specifically to act as a government agency according to Article 14 of the Law for the Regulation and Privatization of the Electricity and Related Water Sector (Sector Law), under which OPWP must remain wholly government-owned. OPWP's obligations are not explicitly guaranteed, but under Article 67 of the Sector Law, the Ministry of Finance must provide adequate financing to enable OPWP to undertake its assigned activities.

We have also revised downward our assessment of OPWP's stand-alone credit profile (SACP) to 'bbb+' from 'a-'. This reflects our view that the ongoing support we factor in from the government to OPWP is still available, but is being provided by a sovereign with a slightly weaker credit profile.

Our satisfactory business risk profile assessment primarily reflects our view of the regulated nature of OPWP's operations. We also see very low industry risk and moderately high country risk.

Our assessment of OPWP's modest financial risk profile stems partly from our assumption that OPWP will not need to raise any material additional long-term debt. We believe that liquidity management is OPWP's main financial risk.

Consequently, we consider OPWP's financial risk profile to be largely predicated on the company's ability to arrange sufficient liquidity in a timely manner to meet working capital deficits while maintaining a robust funds from operations (FFO)-to-debt ratio of more than 50%. We also take into account our projection of the supplementary ratio of EBITDA to interest remaining at 1.5x-2.0x through 2016.

Our base-case scenario for OPWP in 2015-2016 includes the following assumptions:

- Revenue growth of about 3.5%, based on the regulatory payment model and Oman's GDP growth rate.
- EBITDA margins remaining close to 50%.
- A risk weight of 10% for the power purchase agreements (PPAs) (accounted for as leases under International Financial Reporting Standards [IFRS]). The present value of these lease liabilities for 2014 is about Omani rial (OMR) 1,739 million (approximately €4,263 million), of which OMR117.22 million is attributed to finance leases. We risk-weight the entire amount of leases (operating and finance).
- Positive pretax net profits as of 2016, excluding the impact of updates to IFRS that could affect the company's lease reporting.

Liquidity

We regard OPWP's liquidity as adequate, as defined in our criteria. We expect that the company's sources of liquidity will exceed its uses by the minimum threshold of 1.1x for our adequate liquidity category. We also assume that sources will exceed uses even if EBITDA decreases by 10%.

For the 12 months started June 30, 2015, we calculate the following principal liquidity sources:

- Expected cash balances of about OMR6 million;
- Our assumption of FFO of OMR20 million-OMR30 million; and
- An unused amount of committed facilities amounting to of OMR61 million (corresponding to facilities of OMR85 million from Bank of Muscat and OMR50 million from HSBC)

For the same period, we calculate the following principal liquidity uses:

- Debt maturities of OMR14 million; and
- Maximum loan repayments under the working capital facilities, which we estimate to be OMR38 million.

We note that OPWP's working capital funding needs have increased in 2015. As such, the company has been negotiating working capital facilities to meet its working capital needs on a more permanent basis.

Outlook

The negative outlook on OPWP parallels our negative outlook on Oman. Any rating action on Oman would prompt us to take the same action on OPWP.

We currently do not expect our assessments of OPWP's critical role for and integral link with the Omani government to change, meaning that the ratings on OPWP are likely to remain aligned with those on Oman.

Downside scenario

A downgrade of Oman would likely result in a downgrade of OPWP, according to our GRE criteria. The ratings on OPWP could also come under pressure if the company were to deviate from its current practices and engage in long-term borrowing other than to cover working-capital swings. This could lead us to reconsider our view of OPWP's agency role and, in particular, the likelihood of government support. However, we view it as unlikely that OPWP would start to engage in such long-term borrowing.

Upside scenario

The most likely trigger for a revision of the outlook on OWPW to stable would be a similar outlook revision on the sovereign.

Ratings Score Snapshot

Corporate Credit Rating: BBB+/Negative/--

Business risk: Satisfactory

- Country risk: Moderately high
- Industry risk: Very low
- Competitive position: Satisfactory

Financial risk: Modest

- Cash flow/Leverage: Modest

Anchor: bbb+

Modifiers

- Diversification/Portfolio effect: Neutral (no impact)
- Capital structure: Neutral (no impact)
- Financial policy: Neutral (no impact)
- Liquidity: Adequate (no impact)
- Management and governance: Satisfactory (no impact)
- Comparable rating analysis: Neutral (no impact)

Stand-alone credit profile: bbb+

- Likelihood of government support: Almost certain (no impact on SACP)

Related Criteria And Research

Related Criteria

- Rating Government-Related Entities: Methodology And Assumptions, March 25, 2015
- Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- Key Credit Factors For The Regulated Utilities Industry, Nov. 19, 2013
- Methodology: Industry Risk, Nov. 19, 2013
- Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- Corporate Methodology, Nov. 19, 2013
- Corporate Methodology: Ratios And Adjustments, Nov. 19, 2013
- Group Rating Methodology, Nov. 19, 2013
- Methodology For Linking Short-Term And Long-Term Ratings For Corporate, Insurance, And Sovereign Issuers - May 07, 2013
- Methodology: Management And Governance Credit Factors For Corporate Entities And Insurers, Nov. 13, 2012
- Stand-Alone Credit Profiles: One Component Of A Rating, Oct. 1, 2010
- Use Of CreditWatch And Outlooks, Sept. 14, 2009

Ratings List

Downgraded

	To	From
Oman Power and Water Procurement Co. SAOC		

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Corporate Credit Rating

BBB+/Negative/-- A-/Stable/--

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