The Pakistan Credit Rating Agency Limited

NATIONAL REFINERY LIMITED

	NEW [SEP-16]	PREVIOUS [SEP-15]
Long-Term	AA+	AA+
Short-Term	A1+	A1+
Outlook	Stable	Stable

REPORT CONTENTS

SEPTEMBER 2016

Profile

- With a refining capacity of 2.7mln tpa, NRL, the third largest refinery in the country, was incorporated in 1963 and privatized in 2005. AG through its group companies retains the majority stake (51%) in NRL. Other major shareholders include: Islamic Development Bank (15%), NIT's funds (4%), and State Life Insurance Company of Pakistan (4%).

Governance & Management

- NRL's seven member Board of Directors includes four representatives of AG. The remaining three members are independent directors including one nominee representing IDB, one nominee of NIT and one minority shareholder. During the year, Wael G. Pharaon has been replaced by Mr. Mofarrih Saeed H. Alghamdi.
- Dr. Ghaith R. Pharaon, serves as the Chairman of the BoD of NRL. The CEO, Mr. Shuaib A. Malik, a seasoned professional in the oil business, is supported by a team of experienced professionals.

Performance

- During FY16, the company posted an improved performance with a profit of PKR 7,688mln in comparison to PKR 3,708mln in the same period last year. The company's topline declined by ~36% on YoY basis, majorly owing to international crude oil prices. NRL's fuel segment reported a profit of PKR 2,025mln in FY16 as compared to a loss of PKR 81mln in FY15. This increased profitability is in continuation to the FY16 results emanated due to high margins in fuel & lube segments.
- The lube segment continued to remain profitable in line with its previous trend. The volumetric growth on account of higher domestic demand driven by the rising automobile consumption and uptick in industrial activity enhanced the lube segment's profitability on a YoY basis (FY16: 5,530mln; FY15: 3,677mln).
- NRL continues to benefit from interest income (PKR 1,187mln) earned on its bank placements. The stable exchange rate alongwith a reduced finance cost during the period supported the healthy improvement in performance.

Business Strategy

- NRL has initiated projects aimed at enrichment of its product slate in May 2012. These comprises of: a) HSD Desulphurization Project & b) Naphtha Isomerization Project subject to be completed by May'17.
- The company has appointed foreign contractor responsible for the timely execution for the project phases and creates monthly progress reports which is reviewed and monitored by NRL's internal team headed by GM-Special Projects.
- Going forward, the management is focusing on enhancing its product specifications in line with the international standards in motor gasoline and lube base oils.

Working Capital & Cash flows

- NRL maintained its Net Working Capital days (FY16: 29 days, FY15: 30 days) and Gross Net Working Capital Days (FY16: 74 days, FY15: 72 days).
- The company's cash flows remain a function of its profitability. EBITDA amounted to PKR 9,363mln coupled negligible interest payments provides comfort to channel CAPEX & to meet Circular Debt obligations.

Capital Structure

- NRL has commenced its up-gradation projects and financial close for the financing of these projects have been achieved last year. The financing of PKR 24bln under the debt to equity ratio of 65:35 has been retained for a period of 12 years, with a grace period of two years at a rate of 6M Kibor + 175bps.
- Currently ~50% of the project cost has been met through internally generated funds supported by the improvement in refinery's performance. The company plans to start drawing debt from FY17, yet the amount borrowed would be lower in comparison to the initially planned amount.

Rating Rationale

The ratings reflect NRL's strong financial profile emanating from sound cashflows, and healthy liquidity in the form of sizeable bank placements. NRL possesses dominating position in the domestic high margin lube segment alongwith established relationships and product mix. Stabilization in the international LBO market fundamentals bodes well for the company's lube segment performance. The fuel segment showed increased performance on account of stability in the international crude prices benefitting GRMs. NRL has embarked upon value added projects to reinvigorate high margin products through ISOM and DHDS; currently being financed through internal sources with debts to flow. NRL has injected major CAPEX in the projects through internally generated funds resulting in 75% completion of the overall project subject to be commissioned by May'17. NRL's association with the country's only integrated oil group - Attock Group (AG), which on a net basis remains low leveraged - remains a source of comfort.

Key Rating Drivers

The ratings could be impacted by external factors such as prolonged downturn in margins and adverse regulatory changes. The company's ability to maintain its leading position in the lube segment to avoid stress on cash flows remains important for the ratings. Meanwhile, it is crucial that the company maintains its seamless financial profile. Timely completion of the projects in order to avoid any pressure on repayments would be essential.

Industry Snapshot

The global lubricants market is expected to continue its growth momentum with Asia-Pacific as the key region due to enhanced industrial activity in major markets of China and India. This growth in demand coupled with players' ability to hold on some portion of the reduced cost of production due to fall in oil prices helped in improving the lube margins. The local lube sector is largely dominated by NRL (~80%). The remaining domestic demand is met through imports, smuggled products and reclaimed oil to consumption of synthetic lube.

PKR mln

National Refinery Limited

BALANCE SHEET	30-Jun-16	30-Jun-15	30-Jun-14
	Annual	Annual	Annual
Non-Current Assets	**23,704**	**8,161**	**5,311**
Current Assets	**29,956**	**39,777**	**44,462**
Inventory	11,253	13,586	23,857
Trade Receivables	5,297	7,253	10,207
Others	13,406	18,939	10,399
Total Assets	**53,660**	**48,062**	**52,776**
Debt	**-**	**-**	**-**
Short-term	-	-	-
Long-term (Inlc. Current Maturity of long-term debt)	-	-	-
Other shortterm liabilities	16,241	17,163	25,802
Other Longterm Liabilities	598	766	381
Shareholder's Equity	**36,822**	**30,134**	**26,594**
Total Liabilities & Equity	**53,661**	**48,063**	**52,776**
INCOME STATEMENT			
Turnover	**93,788**	**148,457**	**207,403**
Gross Profit	11,043	6,846	3,060
Other Income	499	244	441
Financial Charges	(14)	(1)	(4)
Net Income	**7,688**	**3,709**	**962**
Cashflow Statement			
Free Cashflow from Operations (FCFO)	6,940	3,321	(395)
Net Cash changes in Working Capital	3,044	4,500	(2,738)
Net Cash from Operating Activities	9,984	8,938	(2,290)
Net Cash from InvestingActivities	(14,714)	(467)	(3,532)
Net Cash from Financing Activities	(795)	(1)	(1,195)
Ratio Analysis			
Performance			
Turnover Growth	-36.8%	-28.4%	15.7%
Gross Margin	11.8%	4.6%	1.5%
Net Margin	8.2%	2.5%	0.5%
ROE	27.8%	11.7%	3.5%
Coverages			
Interest Coverage (FCFO/Gross Interest)	565.3	2429.4	-149.8
Core: (FCFO/Gross Interest+CMLTD+Uncovered Total STB)	565.3	2429.4	-149.8
Total: (TCF) / (Gross Interest+CMLTD+Uncovered Total STB)	565.3	3207.6	68.7
Debt Payback (Total LT Debt Including UnCovered Total STBs) / (FCFO- Gross Interes	0.0	0.0	0.0
Liquidity			
Net Cash Cycle (Inventory Days + Receivable Days - Payable Days)	34.5	25.6	28.0
Capital Structure (Total Debt/Total Debt+Equity)	na	na	na

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 National Refinery Limited
Sector Refining
Type of Relationship Solicited

Purpose of the Rating Independent Risk Assessment

Rating History

Dissemination Date	Long Term	Short Term	Outlook	Action
22-Sep-16	AA+	A1+	Stable	Maintain
30-Sep-15	AA+	A1+	Stable	Maintain
14-Nov-14	AA+	A1+	Stable	Maintain
23-Oct-13	AA+	A1+	Stable	Downgrade
2-Nov-12	AAA	A1+	Stable	Maintain
9-Sep-11	AAA	A1+	Stable	Maintain

Related Criteria and Research

Rating Methodology — Corporate Rating Methodology
Sector Research — Refining Sector Viewpoint | Sep-15

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Rating Team Statement

Rating Procedure
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Probability of Default (PD)

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