The Pakistan Credit Rating Agency Limited

ATTOCK REFINERY LIMITED (ARL)

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

REPORT CONTENTS

OCTOBER 2016

Profile

- ARL's refining capacity of 43,000 bpd represents ~10% of the country's overall refining capacity. ARL is part of the country's only integrated oil sector group – Attock Group (AG). AG, through AOC (62%) and its group company Attock Petroleum Limited (APL) [1.6%] retains the majority stake (63%), and management control in ARL.
- **Governance & Management**
- ARL's Board of Directors comprises seven members. Out of these, six are representatives of AG - family - while the remaining one is independent director. During the year, Wael G. Pharon has been replaced by Mr. Mofarrih Saeed H. Alghamdi. The Chairman of the BoD, Mr. Shuaib A. Malik, is also CEO of Attock Oil Group.
- Mr. Adil Khattak, the CEO, has extensive experience in the petroleum sector. During July 2015, he has been re-appointed as CEO of the company till Dec-16. He is supported by an experienced management team which has demonstrated stability over time.

Performance

- During FY16, the company witnessed a significant decline in its revenue by ~48%. This was an outcome of both (a) declining trend in product prices owing to decline in international crude prices and (b) low utilization level achieved during the year on account of tie-in connection activity of the new plants and revamping of existing units.
- The company's GRMs remained low during most part of the year mainly a function of inventory losses on account of decline in crude oil prices in international market resulting in a negative gross profit during the period. The operating expenses largely remained at the same level on a YoY basis.
- ARL's sizeable other income arising from the dividend income due to its strategic investments coupled with interest income on cash placements provided support to the company's performance. PAT (Jun16: PKR816mln, Jun15: PKR1,814mln).

Projects

- ARL, upgradation projects: a) Pre-Flash Unit - enhance refining capacity by 10,400bpd. b) Isomerization Unit – enhance production of PMG; its share in the overall product slate would enhance from 18% to 26%. Meanwhile, the share of Naphtha, a negative margin product for ARL owing to associated freight costs, would decline from 14% to 7%, c) Diesel Hydrosulphurization Project - achieve desulphurization of High Speed Diesel (HSD) to meet EURO II emission standards, and d) Power Generation - addition of 18 MW to power generation capacity. The cost of these projects is ~USD251mln.
- However, due to some unforeseen circumstances related to logistics movement halted in result of political situation coupled with a dispute with govt. over withdrawal of concessionary rate on customs duty (5%) in the Finance Act 2013 the projects could not be commissioned on the revised timeline of June-16. DHDS project has been commissioned during July-16 while the pre-commissioning activities for the rest of the units are underway.

Working Capital & Cash Flow

- During FY16, ARL's cash cycle largely reamiend at the same level on a YoY basic
- ARL's cash flow generation ability remains a function of its profitability and working capital requirements. During FY16, lower profitability constrained the company's cash flows. This resulted in a pressure on coverage's. However, the comfort can be drawn from a sizeable cash balance (June16: PKR 9,683mln) available to the company.

Capital Structure

- The company's equity base stand at PKR 33bln at end Jun-16. After procuring the debt for the expansion projects, the debt/ (debt+equity) ratio of the company stood at 30% as at end FY16.
- ARL has planned to finance the upgradation and expansion projects with the debt to equity ratio of 80:20. The total borrowing amount planned is PKR22bln with a consortium of banks led by Bank Al-Habib Ltd. Debt procured would be repaid in 13 years – 40 equal quarterly payments – with 03 years of grace period.
- After the delay in the commissioning of the projects the revised timeline for the commencing of the principal repayments is 2HFY17. The price is 3M K plus 1.7%. The company has procured ~PKR 15bln as at end-June16.

RATING RATIONALE

The ratings reflect ARL's very strong risk absorption capacity emanating from sizable equity base. ARL's core business remains exposed to the vicissitude of international crude oil and refined product margins. Herein, ARL's product slate with large contribution of high margin products provides comfort. At the same time, ARL's strategic investments and sizable bank placements continue to provide risk absorption capacity and a stable source of income. The ratings also encapsulate ARL's sizable debt for ongoing projects. There has been some delays in the commissioning of projects (ISOM & Pre-flash); hence it is crucial to complete the projects at the earliest. The company has completed DHDS and now benefiting from incremental HSD price. The company can comfortably make few of initial principal repayments from available resources. Subsequently incremental cash-flows would supplement the financial profile. Company's association with the country's only integrated oil group - Attock Group (AG), low leveraged - remains a source of comfort for the ratings.

Key Rating Drivers

The ratings remain dependent on ARL's ability to effectively shield its business profile from volatility in international oil prices. ARL's financial profile, in turn, its ratings, could be negatively impacted from further delay in completion of projects leading to mismatch in projected cash inflows and debt repayments, persistent downturn in refining margins, or un-expected drop in dividend stream. The continuity of deemed duty is crucial.

INDUSTRY

The self sufficiency of United States coupled with a decrease in its reliance on crude import from OPEC and OPEC's decision to maintain its current production level has resulted in an over supplied market. In addition to that, less than expected recovery in the global economy dampened the demand of crude. Resultantly, the oil prices witnessed a steep decline during most of FY16. Significant developments in the global Shale sector, particularly the related infrastructure in US, exerted further pressure on the global crude prices.

PKR mln

Attock Refinery Limited

BALANCE SHEET	30-Jun-16	30-Jun-15	30-Jun-14
	Annual	Annual	Annual
Non-Current Assets	**35,641**	**32,068**	**17,113**
Investments (Incl. associates)	**13,265**	**13,265**	**13,265**
Equity	13,265	13,265	13,265
Debt			
Current Assets	**26,713**	**35,170**	**37,122**
Inventory	6,708	6,574	11,556
Trade Receivables	6,889	15,654	13,239
Others	13,117	12,942	12,327
Total Assets	**75,620**	**80,503**	**67,500**
Debt	**15,164**	**11,659**	**481**
Long-term (Inlc. Current Maturity of long-term debt)	15,164	11,659	481
Other shortterm liabilities	27,266	36,018	35,862
Shareholder's Equity	**33,190**	**32,826**	**31,158**
Total Liabilities & Equity	**75,620**	**80,503**	**67,500**
INCOME STATEMENT			
Turnover	**66,565**	**128,905**	**175,068**
Gross Profit	(902)	553	137
Other Income	2,441	2,775	3,508
Financial Charges	(157)	(413)	(2)
Net Income	**816**	**1,814**	**2,543**
Cashflow Statement			
Free Cashflow from Operations (FCFO)	(2,084)	(2,822)	(1,734)
Net Cash changes in Working Capital	119	3,321	3,172
Net Cash from Operating Activities	(969)	2,619	4,855
Net Cash from InvestingActivities	(2,488)	(14,553)	(4,878)
Net Cash from Financing Activities	3,207	11,361	285
Net Cash generated during the period	(249)	(572)	262
Ratio Analysis			
Performance			
Turnover Growth	-48.4%	-26.4%	7.2%
Gross Margin	-1.4%	0.4%	0.1%
Net Margin	1.2%	1.4%	1.5%
ROE	2.5%	5.7%	8.4%
Coverages			
Debt Service Coverage (x) (FCFO/Gross Interest+CMLTD+Uncovered STB)	-2.9	-2.9	-988.5
Interest Coverage (x) (FCFO/Gross Interest)	-13.3	-6.8	-988.5
Debt Payback (Years) (Total Lt.Debt (excluding Covered Short Term Borrowings) / FCFC	-2.6	-3.6	-0.3
Liquidity			
Short-term Total Leverage (Net Current Assets - STB) / Current Assets	0.6	0.6	0.5
Net Cash Cycle (Inventory Days + Receivable Days - Payable Days)	0.0	0.3	16.0
Capital Structure (Total Debt/Total Debt+Equity)	30.6%	26.2%	1.5%

The Pakistan Credit Rating Agency Limited

STANDARD RATING SCALES & 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.
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 or economic conditions are more likely to impair this capacity.
BB+ BB BB-	**Moderate risk.** Possibility of credit risk developing. There is a possibility of credit risk developing, particularly as a result of adverse economic or business changes over time; however, business or financial alternatives may be available to allow financial commitments to be met.
B+ B B-	**High 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	**Very high 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 within 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, a suspended 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.

Regulatory and Supplementary Disclosure

Rated Entity

Name of Rated Entity Attock Refinery Limited (ARL)
Sector Refining
Type of Relationship Solicited

Purpose of the Rating Independent Risk Assessment
Regulatory Requirement

Rating History

Dissemination Date	Long Term	Short Term	Outlook	Action
13-Oct-16	AA	A1+	Stable	Maintain
13-Oct-15	AA	A1+	Stable	Maintain
20-Nov-14	AA	A1+	Stable	Maintain
7-Oct-13	AA	A1+	Stable	Maintain
19-Oct-12	AA	A1+	Stable	Maintain
7-Sep-11	AA	A1+	Stable	Maintain
6-Oct-09	AA	A1+	Stable	Maintain

Related Criteria and Research

Rating Methodology: Corporate Rating Methodology
Research: Refining Sector Review - 2016

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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.

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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
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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

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