The Pakistan Credit Rating Agency Limited

PAK ARAB REFINERY LIMITED

	NEW [DEC-16]	PREVIOUS [DEC-15]
Long-Term	AAA	AAA
Short-Term	A1+	A1+
Outlook	Stable	Stable

REPORT CONTENTS

DECEMBER 2016

Profile

- Incorporated in 1974 as an unlisted public limited company
- PARCO is a joint venture between the (GoP) and (EAD).
- With a mid-country refinery of 4.5mln tones per annum, PARCO commenced its refining operations in 2000.
- The company operates a network of crude oil-cum-product pipelines running over 2000 kilometers across the country.

Ownership

- PARCO is 60% owned by the GoP, represented by the Ministry of Petroleum and Natural Resources (MPNR) and 40% by the Abu Dhabi Petroleum Investments LLC (ADPI), a majority owned company of Emirate of Abu Dhabi.

Governance

- Nine member board of directors including chairman and the MD
- Five nominees of the GoP, including Chairman and the Managing Director, while remaining four are EAD and OMV nominees.
- Five committees at the Board level, namely Finance, Technical, Bid Evaluation, HR and Audit committees - headed by a board member

Management & Controls

- The company has a well-defined organizational structure with clear segregation of responsibilities.
- The organizational structure of the company is divided into various divisions and departments. All the divisional heads are designated as GM.

Business Risk

- PARCO achieved throughput of ~101%. Although turnover declined by ~36% due to decline in product prices consequent to reduction in international crude oil prices, however the overall sales volume largely remained intact at ~4.6mln metric tons.
- The average GRM remained healthy throughout FY16 at $9.5 per barrel (FY15: $7.6 per barrel).
- The decline in interest income during the year from PKR 2.9bln to PKR 2.6bln was completely overshadowed by rise in dividend income (FY16: PKR 1.9bln; FY15: PKR 1.0bln)
- The finance cost reduced during the year due to settling of long term liabilities and prevailing low interest rate scenario.
- The company posted a net profit after tax of PKR 18.8bln in FY16, 38% higher than FY15. Going forward, PARCO is planning to increase the capacity of;
    - The refinery by additional 20,000 barrels per day.
    - MFM Pipeline from 3 million tons to 7 million tons
- Keeping in view the demand/supply situation of refined products, a new refinery project is under evaluation of PARCO.

Financial Risk

- During the year crude oil prices hit its historical low that bodes well for the PARCO as lower oil prices helped the entity to engage minimum assets to fund its working capital needs.
- During the year crude oil prices witnessed a dip of 18% that translated into a decline in inventory value of 28%. The rippled down effect was also reflected in decrease in receivables and payables by 16% and 33%.
- The increased gearing of PARCO from 3.0% in FY15 to 10.7% in FY16 was a result of temporary short term borrowing repaid in July 2016.

RATING RATIONALE

The ratings reflect PARCO's predominantly sovereign ownership structure- owned by the Government of Pakistan (GoP) (60%) and Abu Dhabi Petroleum Investments LLC (40%- a majority owned company of Emirate of Abu Dhabi) (EAD). Additionally, it enjoys strategic importance to the GoP for its socio-economic policies and its quest of reducing the import bill. The company's low business risk emanates from its leading market position, strong demand of its products, and its advanced plant technology. The business fundamentals also derive support from high premium product mix and diversified revenue stream. At the same time, the ratings recognize the company's ability to manage its financial profile. Also reflected in the ratings is PARCO's strengthened position in midstream and downstream sector with organic growth and acquisitions.

KEY RATING DRIVERS

Effective management of upcoming and consistency in Government policies remain critical for the ratings. The ratings are dependent on sustained competitive positioning of the company.

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PAK ARAB REFINERY LIMITED

PKR mln

BALANCE SHEET	30-Sep-16	30-Jun-16	30-Jun-15
	Annual	*Annual*	*Annual*
Non-Current Assets	21,496	21,978	25,015
Investments	58,156	61,616	44,053
Inventories	17,343	17,832	24,792
Current Assets	27,296	24,252	32,633
Total Assets	124,291	125,678	126,493
Borrowings	1,046	1,045	1,523
Total Liabilities (excluding long term borrowings)	45,459	52,545	43,262
Shareholders' Equity	77,786	72,088	81,708
Total Liabilities & Equity	124,291	125,678	126,493

PROFIT & LOSS ACCOUNT	30-Sep-16	30-Jun-16	30-Jun-15
Turnover	55,525	198,099	307,285
Gross Profit	7,708	27,413	19,927
Interest Income	-	2,623	2,933
Interest Expense	(24)	(663)	(1,009)
Exchange Gain / (Loss)	(240)	162	(1,065)
Net Income	5,699	18,831	13,647

CASHFLOW STATEMENT	30-Sep-16	30-Jun-16	30-Jun-15
EBITDA	8,637	29,743	21,468
Free Cashflow from Operations (FCFO)	7,137	20,974	12,989
Net Cash provided by Operating Activities	14,629	24,636	17,476
Net Cash (used in) / available from investing activities	(361)	2,143	(2,673)
Cashflow from financing activities	(14,288)	(14,255)	(11,167)

RATIO ANALYSIS	30-Sep-16	30-Jun-16	30-Jun-15
Gross Margin	13.9%	13.8%	6.5%
Net Profit Margin	10.3%	9.5%	4.4%
Debt Service Coverage (times)	22.5	17.7	7.0
Interest Coverage (times)	112.0	13.0	13.0
Net Cash Cycle (Days)	14.0	14.0	14.0
Debt : Equity	21%	3%	3%

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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

Rating	Definition
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 but may stay in abeyance for long.

Withdrawn
A rating is withdrawn on a) termination of rating mandate, b) cessation of underlying entity, or c) the debt instrument is redeemed.

Disclaimer: PACRA's ratings are an assessment of the credit standing of entities in Pakistan. They do not take into account the potential transfer / convertibility risk that may exist for foreign currency creditors. PACRA's rating is not a recommendation to purchase, sell or hold a security, in as much as it does not comment on the security's market price or suitability for a particular investor.

Regulatory and Supplementary Disclosure

Name of Issuer	Pak Arab 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
30-Dec-16	AAA	A1+	Stable	Maintain
31-Dec-15	AAA	A1+	Stable	Maintain
13-Jan-15	AAA	A1+	Stable	Maintain
15-Jan-14	AAA	A1+	Stable	Maintain
3-Jan-13	AAA	A1+	Stable	Maintain
27-Mar-12	AAA	A1+	Stable	Maintain
29-Nov-10	AAA	A1+	Stable	Maintain

Related Criteria and Research

Rating Methodology	Corporate Rating Methodology
Sector Research	Pakistan Refining Industry An Overview - Oct 16

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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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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

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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

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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