The Pakistan Credit Rating Agency Limited

PAKISTAN REFINERY LIMITED | TFC II

INSTRUMENT RATINGS REPORT

	NEW [JUN-17]	PREVIOUS [JUN-16]
Long-Term	A	A
Short-Term	-	-
Outlook	Stable	Stable

REPORT CONTENTS

JUNE 2017

Debt Instrument

- TFC II, carrying fixed profit rate of 10.75%, has a tenor of 5 years and will be due for maturity in Dec'18. Although principal repayment is at maturity, these instruments carry perpetual Put option. TFCs is secured by way of Hypothecation of a) Stocks and Receivables & b) Fixed Assets with certain margin

Profile

- Pakistan Refinery Limited (PRL), having refining capacity of 2.1mln tons per annum, is operational since Oct'62. Majority shareholding in PRL is held by Shell Petroleum Company Limited, UK, and (30%) Pakistan State Oil Company Limited (22.5%), HASCOL (14%).
- Chevron intends to sell its entire stock in the company. The transaction is currently under litigation on the basis of shareholder agreement between Class B shareholders.
- Shell has offered 26.67% stake in the company to PSO. The transaction is currently under regulatory approvals. Once concluded, PSO will become major shareholder in the company.
- The company has eleven member board (including the CEO) – six representing sponsoring companies (currently three from PSO, two from Shell and one Chevron), two directors from Hascol and one independent director.
- Mr. Aftab Husain, PRL's CEO, Chemical Engineer has been associated with PRL for over three decades. He is supported by a team of qualified and competent individuals.

Performance

- During 9MFY17, PRL witnessed a mariginal increase in its turnover on a YoY basis ~1% mainly on account of an increase in the prices of petroleum products in the international market during most part of the period.
- Marginal increase in the overall operational expenses alongwith the finance cost exerted negativity on the bottomline. However, the positive contribution to GRMs due to ISOM helped in generating healthy profitability on a YoY basis (9MFY17: PKR 1,066mln, 9MFY16: of PKR860mln).

Business Strategy

- Going forward, the refinery is continuing to work on the Refinery Expansion and Up-gradation Project (REUP). The Diesel Hydrodesulphurization Unit (DHDS), which is part of the REUP will make the refinery become compliant with the Government of Pakistan's requirement to produce EURO II compliant Diesel. The company has received a feasibility report prepared by an international consultant engaged for evaluating different technological variants for expansion and up-gradation of the refinery including installation of DHDS

Working Capital & Cashflows

- PRL's working capital requirement emanate from its need to finance its inventory and circular debt, which usually results in net receivable position to the company.
- PRL's cash flow generation ability remains a function of its profitability and working capital requirements. During 9MFY17, healthy profitability helped in improving the company's cash flows. The company's coverages remained positive yet remained below the adequate level

.Capital Structure

- PRL raised its equity during last year through a right issue amounting to PKR 2.59bln. The subscription money was received against the planned right issue of PKR 2.8bln. The remaining amount of PKR 210mln is subject to a restraining order that has been obtained from the court by one of the class B shareholder against the other class B shareholder.
- PRL has a long term loan of PKR 2bln obtained for an up-gradation project (Isomerization). The said loan will be repayable in ten semi-annual payments with a maturity of seven years @ 6MK+175bps. The repayments would commence during FY18.

RATING RATIONALE

The ratings reflect strong business profile of PRL emanating from its sustainable operational history, strong demand of its products, and its strategic importance in the domestic context. The design of PRL's plant offers relatively limited flexibility; in turn, low margin and high exposure to volatile dynamics of international crude oil and refinery product pricing. However, with the successful commissioning of Isomerization plant, the company experienced volumetric growth in petrol, a high-margin product, which boosted profitability. The incremental cashflows are adequate considering size of the related debt obligations. In addition, the favorable oil prices supplemented the profitability and hence cashflows. The company is targeting up – gradation (Hydro-desulphurisation) and expansion (enhancing refinery existing capacity) projects.

KEY RATING DRIVERS

The ratings could be impacted by prolonged constrain in refining margins and/or adverse changes in the existing regulatory framework leading to depressed core cashflows. The company has conducted a leveraged up-gradation of its operating platform. Since repayment pattern is aligned to expected cash flows, timely settlement of obligation is important. Prudent management of new borrowings related to expansion, thereby impacting coverages, is important.

PKR mln

Pakistan Refinery Limited

BALANCE SHEET	30-Mar-17	30-Jun-16	30-Mar-16	30-Jun-15
	3QFY17	Annual	3QFY16	Annual
Non-Current Assets	**12,377**	**12,390**	**12,163**	**12,601**
Investments (Incl. associates)	**87**	**85**	**82**	**91**
Equity	87	85	82	91
Current Assets	**15,320**	**12,302**	**22,487**	**18,061**
Inventory	8,027	5,090	4,378	5,516
Trade Receivables	5,223	5,211	12,169	6,231
Others	2,070	2,001	5,941	6,314
Total Assets	**27,785**	**24,777**	**34,733**	**30,753**
Debt	**10,453**	**10,561**	**20,117**	**11,316**
Short-term	8,218	6,594	16,129	7,194
Long-term (Inlc. Current Maturity of long-term debt)	2,235	3,967	3,988	4,123
Other shortterm liabilities	13,941	11,787	11,831	17,514
Other Longterm Liabilities	246	261	140	138
Shareholder's Equity	**3,145**	**2,167**	**2,645**	**1,785**
Total Liabilities & Equity	**27,785**	**24,777**	**34,733**	**30,753**
INCOME STATEMENT				
Turnover	**50,011**	**64,733**	**49,754**	**91,175**
Gross Profit	1,754	1,990	1,936	(677)
Net Other Income	381	(140)	83	187
Financial Charges	(456)	(909)	(688)	(707)
Net Income	**1,066**	**283**	**860**	**(1,182)**
Cashflow Statement				
Free Cashflow from Operations (FCFO)	2,255	2,050	2,168	(1,017)
Net Cash changes in Working Capital	(721)	(2,059)	(8,931)	2,021
Net Cash from Operating Activities	1,141	(1,071)	(7,383)	(56)
Net Cash from InvestingActivities	(762)	(520)	(266)	(4,616)
Net Cash from Financing Activities	(295)	(637)	9,010	5,195
Ratio Analysis				
Performance				
Turnover Growth	0.5%	-29.0%	-29.7%	-35.9%
Gross Margin	3.5%	3.1%	3.9%	-0.7%
Net Margin	2.1%	0.4%	1.7%	-1.3%
ROE	45.2%	11.7%	46.0%	-68.3%
Coverages				
Interest Coverage (FCFO/Gross Interest)	4.9	2.3	3.2	-1.4
Core: (FCFO/Gross Interest+CMLTD+Uncovered Total STB)	0.4	0.2	0.3	-0.1
Total: (TCF) / (Gross Interest+CMLTD+Uncovered Total STB)	0.4	0.2	0.3	-0.1
Debt Payback (Total LT Debt Incl. Uncovered Total STBs) / (FCFO-Gross Int.)	3.8	8.8	4.8	-6.2
Liquidity				
Net Cash Cycle (Inventory Days + Receivable Days - Payable Days)	0	0	13	2
Capital Structure (Total Debt/Total Debt+Equity)	0.0%	0.0%	88.4%	86.4%

CREDIT 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.
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-	**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**. 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.

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'.

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. A watch should be resolved within foreseeable future, but may continue if underlying circumstances are not settled. Rating Watch may accompany Outlook of the respective opinion.

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, e) the entity/issuer defaults., or/and f) PACRA finds it impractical to surveill the opinion due to lack of requisite information