The Pakistan Credit Rating Agency Limited

Rating Report

Orient Petroleum Inc. (Pakistan Branch)

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
21-Dec-2023	A-	A2	Stable	Maintain	-
21-Dec-2022	A-	A2	Stable	Maintain	-
22-Dec-2021	A-	A2	Stable	Maintain	-
22-Dec-2020	A-	A2	Stable	Initial	-

Rating Rationale and Key Rating Drivers

Pakistan's E&P segment, including 10 domestic and 14 foreign companies, operates with 24 rigs actively deployed for drilling with ~124 active exploration licenses as of FY22 by the Ministry of Energy and Petroleum. There is an average of ~3 wells per 1,000 sq. km for exploratory acreage. Currently, ~1,114 exploration wells and ~1,484 appraisal/development well drilled as of Dec-21. Oil production and Gas production in Pakistan stood at 81,496bbl per day and 3,403mmcfd per day, respectively.
Orient Petroleum Inc. ('Orient' or 'the Company') drives its strength from its Group companies that include Orient Petroleum Pty Limited (OPPL), Zaver Petroleum Corporation (ZPCL), OPI Gas (Pvt.) Limited and Hashwani Hotels Limited (HHL) which owns and operate chain of Marriott hotels in Pakistan. Orient is engaged in the exploration, development and production of oil and natural gas reserves. Currently, the Company holds a working interest in six production lease agreements - Ratana, Dhurnal, Bhangali, Sinjhoro, Mehar & Sofiya - and eight exploration licenses - namely Sakhi Sarwar, Marwat, Harani South, Saruna, Kohlu, Sinjhoro, Waziristan & Mehar block. Recent discovery in Waziristan block is the major breakthrough for the Company. In Waziristan Block Company holds 10% non-operated working interest. Furthermore, the Company successfully secured plant rental agreement for two years, where the Company shall provide its plant on a rental basis to Waziristan block along with its operations and management. The Company achieved growth of 78% in its top line which is mainly attributable to a conducive business environment in E&P sector worldwide. On the operational front, Orient production reports identified crude oil, gas & LPG production of 153,234bbl; 2,505mmbtu and 6,811MT, respectively, from Jul-22 to Jun-23. Overall, the Company's business margins posted growth. However, net margins remain low due to higher interest cost along with exchange loss. The Company drives strength from risk-adjusted recoverable reserves both from its production and development and exploration assets. As conceived, increase in volumes, going forward, will lead to better profitability. However, executional strategies and expected synergies remain crucial. On the financial risk front, the Company is adequately leveraged, with a moderate working capital cycle. However, coverages remain strong. Going forward, financial discipline along with better governance framework remains pivotal for the ratings.

The ratings are dependent on the sustained relative positioning of the Company. Volatility in topline and profitability remains key concerns. The ratings would take positive benefit from the increase in volumes handled by the Company. However, financial discipline along with the sponsor's support are imperative to ratings, while maintaining the coverage ratios.

Disclosure

Name of Rated Entity	Orient Petroleum Inc. (Pakistan Branch)
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology | Corporate Rating(Jul-23),Methodology | Correlation Between Long-term & Short-term Rating Scales(Jul-23),Methodology | Rating Modifiers(Apr-23)
Related Research	Sector Study | Oil Marketing Companies(Nov-22)
Rating Analysts	Faiqa Qamar | faiqa.qamar@pacra.com | +92-42-35869504

Profile

Legal Structure Orient Petroleum Inc. ('the Company' or 'Orient Petroleum') is incorporated in Cayman Islands. The Company operates in Pakistan through its branch office in Islamabad.

Background Occidental Pakistan Inc., a USA-based organization, has been working in Pakistan's oil and gas exploration segment since 1979. In five years, the Company made Pakistan's largest oil discovery from its Dhurnal field in Potwar Basin, Punjab. The discovery had over 150mln barrels of oil and produced over 22,000 barrels of oil per day. In 1995, Hashoo Group ('the Group') acquired Occidental Pakistan Inc and renamed it to Orient Petroleum Inc.

Operations Orient Petroleum is engaged in the exploration, development, production and sale of crude oil, natural gas and liquefied petroleum gas (LPG). The Company operates eight exploration licenses and six development and production blocks in Pakistan.

Ownership

Ownership Structure The Group owns the Company through its two holding companies, Zaver Petroleum (~55%) and First Global Investment Holding Ltd (~45%).

Stability Since ownership resides with the sponsoring Group, thus, ownership is deemed stable, going forward.

Business Acumen The Group holds stakes in multiple business segments like hospitality, oil & gas exploration and production. The business acumen of the Sponsors - Mr. Hassan Ai Hashwani - and the ability to channel and execute the defined business strategies remain incomparable.

Financial Strength The Group holds considerable financial footing to support the Company in destress, if needs be.

Governance

Board Structure The Board comprises four members, two Executives and two Non-Executive Directors. Both, Non-Executive Directors are from the Sponsoring family.

Members' Profile Mr. Sadrud-din-Hashwani, the founder and Chairman of the Group, provides guidance with over 43 years of experience. All members of BoD have substantial experience in the relevant domain.

Board Effectiveness The Board is actively involved in the supervision and oversight of management to make informed decisions, leading to the entity achieving its objectives, and supported by the technical advisory committee, comprising Executive Directors. The Board conducts regular meetings with majority attendance to discuss various aspects of the Company.

Financial Transparency External Auditors of the Company, M/s Grant Thornton Anjum Rahman, has expressed an unqualified opinion on financial statements as of Dec-22.

Management

Organizational Structure The Company's operations are bifurcated into Reservoir Engineering, Exploration, Surface Operations, Drilling, Petroleum Engineering, Finance, Admin, MIS, HR, Internal Audit and Procurement & Supply Chain. All Departmental heads report to the CEO, who then reports to the BoD.

Management Team Mr. Kamran Ahmed, the CEO of Orient Petroleum, has more than 3 decades of experience in investment banking and the oil & gas industry. Mr. Kamran's has been a part of Shell Pakistan and Islamic Investment Bank Ltd and an integral part of the Group for two decades. He leads a team of seasoned professionals.

Effectiveness The Company's management is crucial in empowering the operational team to attain targeted results and ensuring adherence to a systematic decision-making process. However, no committees exist at the management level.

MIS Oracle ERP has been implemented at Orient Petroleum, which provides real-time end-to-end integrated solution for all operations including financial, purchasing, inventory, HRMS, allocation, payroll and approval management system. OPI has a dedicated team of professionals for in-house development, customization and maintenance of Oracle applications for Oil & Gas specific requirements.

Control Environment The Company has placed an effective internal audit department forming SoPs and ensuring their compliance. The department directly reports to the Board.

Business Risk

Industry Dynamics In Pakistan, 10 domestic and 14 Foreign companies are operating with 24 rigs actively deployed for drilling, ~124 active exploration licenses as of FY22. Pakistan has an average of ~3 wells per 1,000 sq. km of exploratory acreage. Currently, ~1,114 exploration wells and 1,484 appraisal/development well drilled as of Dec'21. Oil production and Gas production in Pakistan stood at 81,496 Barrels of oil per day and 3,403 million cubic feet per day respectively. Exploration and production of hydrocarbons require high levels of capital expenditures and is a high-risk venture.

Relative Position At present, there are 14 foreign and 10 local companies operating in Pakistan. Market share is dominated by state-owned Oil and Gas Development Company Limited (OGDCL). The other large-tier competitor companies comprise Pakistan Petroleum Limited, Mari Petroleum Limited and Pakistan Oil Field etc. Mid-tier companies include MOL and Orient Petroleum Inc.

Revenues The Company's revenue mix comprises Condensate ~45% followed by Gas ~32%, LPG ~15% and Crude oil ~8%. During CY22, the Company observed ~78% growth in the topline (CY22: ~PKR 5,223mln, CY21: ~PKR 2,936mln). The increase is linked to higher volumetric sales coupled with an increase in output pricing. Further, during 6MCY23, the topline of the Company surged to ~PKR 3,117mln.

Margins During CY22, the gross margin of the Company stood at ~76% (CY21: ~74%) due to an increase in the output (oil and gas) prices in the international market. The trickle-down impact was observed in the operating margins which surged to ~39% during CY22 (CY21: ~29%). Owing to high finance cost, exchange translation loss and deferred taxation during CY22, the Company reported a net loss of ~PKR 741mln during CY22 (CY21: ~PKR 277mln). During 6MCY23, the gross margin of the Company stood at ~74%, the operating profit margin of the Company surged to ~39%, whereas, the net profit margin of the Company stood at ~40%.

Sustainability The management is proactively addressing previous security concerns to resume operations in the Marwat block recognizing its potential to significantly boost the Company's performance.

Financial Risk

Working Capital In CY22, the Company experienced an increase in net working capital days reaching to ~84 days (CY21: ~52 days). This surge was primarily attributed to a high trade receivable days (CY22: ~146 days, CY21: ~136 days). Conversely, trade payable days decreased to ~63 days in CY22 from ~84 days in CY21. In 6MCY23, net working capital days continued to rise, reaching around ~123 days, driven by high trade receivables. The Company's trade receivables increased to ~PKR 3,412mln, resulting in an extension of trade receivables days to ~184 days. In contrast, trade payable days were reduced to ~61 days. During CY22, the short-term financing of the Company surged by 95% (CY22: PKR 862mln, CY21: PKR 442mln) due to stretched working capital. Orient maintains Short term trade leverage of 35% in CY22 (CY21: -10%). During 6MCY23 the Company's short-term borrowings stood at ~PKR 263mln.

Coverages The Company's cash flows are linked to profitability. The internal cash generation, primarily stemming from hydrocarbon sales and income from deposits, effectively fulfills the Company's liquidity needs. As at CY22, the free cash flow from operations (FCFO) experienced a notable increase, surging to ~PKR 3,377mln, marking a growth of about ~99% (CY21: ~PKR 1,699mln). This enhancement in FCFO contributed to an improved interest coverage ratio, reaching ~2.9x in CY22 (CY21: ~2.4x). In 6MCY23, interest coverage ratio of the company stood at ~2.4x.

Capitalization The Company's capital structure exhibited fluctuating patterns, with the debt-to-equity ratio at ~43% as of CY22 (CY21: ~37%). The uptake in the debt-to-equity ratio is primarily attributed to the rise in long-term borrowings, reaching around ~PKR 2,240mln as of CY22 (CY21: ~PKR 2,240mln). The short-term borrowings amounted to ~PKR 862mln as of CY22 (CY21: ~PKR 442mln). The Company equity decreased to ~PKR 5,295mln as of CY22 (CY21: ~PKR 6,560mln), with the decline linked to a reduction in revaluation surplus. As of 6MCY23, the debt-to-equity ratio increased to ~54%, while equity saw an increase to around ~PKR 5,791mln.

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Financial Summary
PKR mln

Orient Petroleum Inc.	Jun-23	Dec-22	Dec-21	Dec-20
Oil Exploration & Production	6M	12M	12M	12M
A BALANCE SHEET				
1 Non-Current Assets	19,054	18,042	16,131	11,983
2 Investments	-	-	-	-
3 Related Party Exposure	1,782	1,898	1,930	2,190
4 Current Assets	8,882	6,646	4,016	3,518
a Inventories	*14*	*14*	*15*	*6*
b Trade Receivables	*3,412*	*2,860*	*1,309*	*866*
5 Total Assets	29,718	26,585	22,077	17,691
6 Current Liabilities	5,698	6,080	3,465	2,756
a Trade Payables	*1,192*	*895*	*912*	*444*
7 Borrowings	6,732	4,004	3,804	3,509
8 Related Party Exposure	-	-	-	-
9 Non-Current Liabilities	11,498	11,207	8,247	7,181
10 Net Assets	5,791	5,295	6,560	4,245
11 Shareholders' Equity	5,791	5,295	6,560	4,240
B INCOME STATEMENT				
1 Sales	3,117	5,223	2,936	2,385
a Cost of Good Sold	*(796)*	*(1,227)*	*(758)*	*(782)*
2 Gross Profit	2,321	3,996	2,178	1,602
a Operating Expenses	(1,091)	(1,956)	(1,318)	(1,165)
3 Operating Profit	1,230	2,040	860	438
a Non Operating Income or (Expense)	*775*	*(606)*	*(192)*	*(45)*
4 Profit or (Loss) before Interest and Tax	2,005	1,434	668	393
a Total Finance Cost	*(758)*	*(1,170)*	*(705)*	*(683)*
b Taxation	-	*(1,005)*	*314*	*970*
6 Net Income Or (Loss)	1,247	(741)	277	679
C CASH FLOW STATEMENT				
a Free Cash Flows from Operations (FCFO)	*2,035*	*3,371*	*1,695*	*1,245*
b Net Cash from Operating Activities before Working Capital Changes	*2,035*	*3,382*	*1,701*	*1,255*
c Changes in Working Capital	*(422)*	*(7)*	*168*	*138*
1 Net Cash provided by Operating Activities	1,614	3,375	1,869	1,393
2 Net Cash (Used in) or Available From Investing Activities	(1,609)	(3,125)	(2,128)	(827)
3 Net Cash (Used in) or Available From Financing Activities	2,135	(8)	20	(2,045)
4 Net Cash generated or (Used) during the period	2,140	242	(238)	(1,479)
D RATIO ANALYSIS				
1 Performance				
a Sales Growth (for the period)	19.4%	77.9%	23.1%	-21.5%
b Gross Profit Margin	74.5%	76.5%	74.2%	67.2%
c Net Profit Margin	40.0%	-14.2%	9.4%	28.5%
d Cash Conversion Efficiency (FCFO adjusted for Working Capital/Sales)	51.8%	64.4%	63.5%	58.0%
*e Return on Equity [Net Profit Margin * Asset Turnover * (Total Assets/Sh*	45.0%	-12.5%	5.1%	14.4%
2 Working Capital Management				
a Gross Working Capital (Average Days)	184	147	136	155
b Net Working Capital (Average Days)	123	84	52	77
c Current Ratio (Current Assets / Current Liabilities)	1.6	1.1	1.2	1.3
3 Coverages				
a EBITDA / Finance Cost	2.4	2.9	2.4	1.8
b FCFO / Finance Cost+CMLTB+Excess STB	2.0	1.4	1.2	0.7
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)	2.5	1.6	3.4	5.7
4 Capital Structure				
a Total Borrowings / (Total Borrowings+Shareholders' Equity)	53.8%	43.1%	36.7%	45.3%
b Interest or Markup Payable (Days)	0.0	0.0	0.0	0.0
c Entity Average Borrowing Rate	28.3%	30.0%	19.3%	17.7%

Credit Rating

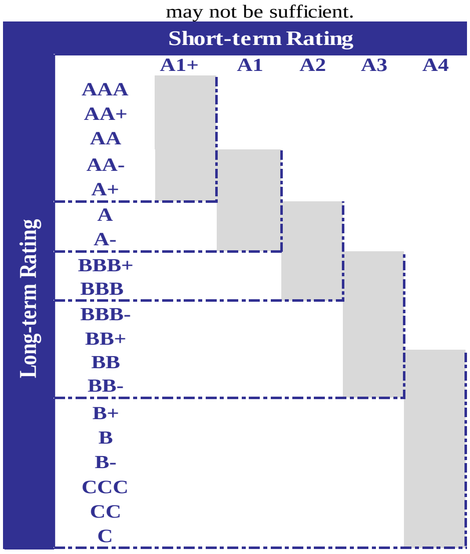
Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

Long-term Rating

Scale	Definition
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 Rating

Scale	Definition
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
A4	The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions. Liquidity may not be sufficient.



**The correlation shown is indicative and, in certain cases, may not hold.*

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 some material identifiable event with indeterminable rating implications. 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 rating 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) the debt instrument is redeemed, c) the rating remains suspended for six months, d) the entity/issuer defaults., or/and e) PACRA finds it impractical to surveill the opinion due to lack of requisite information.

Harmonization A change in rating due to revision in applicable methodology or underlying scale.

Surveillance. Surveillance on a publicly disseminated rating opinion is carried out on an ongoing basis till it is formally suspended or withdrawn. A comprehensive surveillance of rating opinion is carried out at least once every six months. However, a rating opinion may be reviewed in the intervening period if it is necessitated by any material happening.

Note. This scale is applicable to the following methodology(s):

a) Broker Entity Rating
b) Corporate Rating
c) Debt Instrument Rating
d) Financial Institution Rating
e) Holding Company Rating
f) Independent Power Producer Rating
g) Microfinance Institution Rating
h) Non-Banking Finance Companies Rating

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(Credit Rating Companies Regulations,2016)

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Conduct of Business
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(13) PACRA does not provide consultancy/advisory services or other services to any of its customers or to any of its customers' associated companies and associated undertakings that is being rated or has been rated by it during the preceding three years unless it has adequate mechanism in place ensuring that provision of such services does not lead to a conflict of interest situation with its rating activities; | Chapter III; 12-2-(d)
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(20) PACRA initiates immediate review of the outstanding rating upon becoming aware of any information that may reasonably be expected to result in downgrading of the rating; | Chapter III | 17-(c)
(21) PACRA engages with the issuer and the debt securities trustee, to remain updated on all information pertaining to the rating of the entity/instrument;| Chapter III | 17-(d)
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(22) 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; | Chapter III | 14-3(f)(vii)
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