



The Pakistan Credit Rating Agency Limited

Rating Report

Pak-Arab Pipeline Company Limited

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Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
02-Jun-2023	AAA	A1+	Stable	Maintain	-
10-Jun-2022	AAA	A1+	Stable	Maintain	-
10-Jun-2021	AAA	A1+	Stable	Maintain	-
10-Jun-2020	AAA	A1+	Stable	Maintain	-
23-Nov-2019	AAA	A1+	Stable	Maintain	-
24-May-2019	AAA	A1+	Stable	Maintain	-
23-Nov-2018	AAA	A1+	Stable	Initial	-

Rating Rationale and Key Rating Drivers

Pak Arab Pipeline Company Ltd. (the Company) owns and operates a dedicated pipeline network which is used to transport White Oil. The pipeline network is 786KM long which extends from Port Qasim and Kaemari to mid-country Mehmodkot and from there to Machike. The pipeline capacity to transport is 8mln tons of the commodity/annum, which can be increased up to 12mln tons/annum, considered to be sufficient to meet the upcountry's demand. Its unique business model provides basic infrastructure for smooth running and transportation of White Oil through mid-country. Therefore, its strategic importance at country level is eminent. The pipeline has been upgraded to transport Motor Gasoline (MOGAS) in addition of High Speed Diesel (HSD) in Nov'21. This upgradation is debt driven; from syndicate local debt and foreign borrowings. The Company has successfully started its repayment as per schedule and going forward leverage is expected to reduce. The ratings are reflective of PAPCO's strategic importance to the country and its distinctive business model deriving its strength from a US\$ based tariff structure, providing sustainability to the Company's profit and certain cushion against exchange rate fluctuations. Market for petroleum products (POL) declined in 3QFY23, business volumes of PAPCO also displayed a similar trend capacity utilization reduced at ~28% including 8% for MOGAS in 3QFY23 (1HFY22: ~50%). The macro economic factors lead to slow down in economic activity which resulted in lower demand of petroleum products. In addition to that the upliftment of at least 35% of MOGAS transported through pipeline by authority may have negatively impacted the company's throughput and the impact of which going forward is yet to be seen. The liquidity profile of the company is considered as strong due to its sizable short-term investment book on the balance sheet and its cash richness. The cash flows of the company remain persistently strong, stemming from formidable profitability margins. The company's governance structure derives full benefit from its association with PARCO, which also deposes its functionaries in PAPCO, with Shell Pakistan Limited nominating the CFO.

The ratings are dependent on sustained business model and its share in the overall country's petroleum movement. Sustainability in system share remains vital for the ratings. Execution of contracts and timely delivery of products is also important. Meanwhile, adherence to strong performance indicators is imperative.

Disclosure

Name of Rated Entity	Pak-Arab Pipeline Company Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology Corporate Rating(Jun-22),Methodology Correlation Between Long-term & Short-term Rating Scales(Jun-22),Methodology Rating Modifiers(Jun-22)
Related Research	Sector Study Pipeline Networks(Oct-22)
Rating Analysts	Anam Waqas Ghayour anam.waqas@pacra.com +92-42-35869504

Profile

Legal Structure Incorporated in the year 2000, Pak Arab Pipeline Company Limited (PAPCO) is a public unlisted Company.

Background A benchmark laid in the form of Public-Private partnership between top OMCs of the country: Shell Pakistan Limited, PSO and TOTAL PARCO Marketing Limited (formerly known as Chevron Pakistan Limited) and PARCO, to build and operate a US\$ 480 million cross-country pipeline system for transporting High-Speed Diesel from Karachi ports to upcountry locations. Recently, PAPCO has completed the up-gradation of its White Oil Pipeline (WOP). The up-gradation has enabled the pipeline to transport MOGAS along with HSD.

Operations PAPCO operates a state-of-the-art cross-country pipeline system, White Oil Pipeline Project (WOPP), to transport refined High Speed Diesel from Karachi ports to up-country. Pipeline was commissioned in March 2005, comprising 786 Km of 26" dia cross-country pipeline, storage tanks, pumps and other allied facilities. PAPCO is a successful fuel carrier for the country. The pipeline network is entirely underground based except where there are water streams.

Ownership

Ownership Structure PAPCO's majority holding lies in the hands of PARCO - 62% (which is majorly owned by GoP) while remaining by Shell Pakistan Limited (26%) and PSO (12%). Initially, there was a signing of Implementation Agreement (IA) between Government of Pakistan and PARCO, PAPCO & Emirate of Abu Dhabi acclaims strong ownership structure for the company.

Stability Prolific backing of its sponsors denotes strong foothold in the oil transportation market.

Business Acumen PARCO holding in PAPCO is part of its strategic alliance whereas, the entire operational efficacy flows collectively from its partners.

Financial Strength Profound ownership flows from its main sponsors-PARCO, anchoring as the backbone of PAPCO.

Governance

Board Structure Company's overall control is overseen by ten-member Board of Directors (BoD), representing all the shareholders. Mr. Capt. (Retd.) Muhammad Mahmood is the new chairman, nominated in the BOD meeting held on Nov 18, 2022.

Members' Profile Mr. Amr is the Chief Executive Officer and is nominated by PARCO, Mr. Amr holds a bachelors degree in Mechanical Engineering and is also an MBA. He possesses a vast experience of more than three decades and joined PARCO in December 2020.

Board Effectiveness Having audit committee as part of the Company's board, keeps an oversight on overall business. The company conducted four board meetings witnessing good level of attendance.

Financial Transparency PAPCO's external auditor, KPMG Taseer Hadi & Co. (appointed for June 2023 FS audit), however, June 30, 2022 annual audit was conducted by EY. They have expressed an unqualified opinion on the company's financial statement as of June 22.

Management

Organizational Structure The Company follows a regime of formal well-defined organizational structure with the flare of segregated departments.

Management Team PAPCO has maintained a high profile decorum of its management. Mr. Syed Muhammad Haris, Chief Financial Officer (CFO), possesses more than two decades of experience in related field. He took as the Chief Financial Officer PAPCO in April 21 and has been aptly deploying his expertise since then. He is nominated by Shell.

Effectiveness The entire quorum of management is well-qualified, having ties with the group since long. To affirm effectiveness, all reporting lines fall to CEO.

MIS PAPCO maintains sophisticated IT infrastructure throughout its operational lines, with three types of software including ERP.

Control Environment PAPCO enjoys the supremacy of possessing expertise from its entire group. Quality control reports are generated on regular basis and reviewed by senior engineers on daily basis as well as weekly/monthly basis.

Business Risk

Industry Dynamics In Pakistan, a major portion of oil products is transported through roads. In FY22, ~70% of total oil products were moved by roads followed by pipeline ~28%, and ~2% by railways. Moreover, with the start of MOGAS transport through the pipeline from Nov 21, overall throughput through the pipeline has been improved. Under Pakistan's entire universe of petroleum products, MOGAS constitutes ~40% of the total demand.

Relative Position PAPCO bags the title of being the sole HSD and MOGAS transporter through pipeline network in the country. The company has a pivotal geographic presence in Pakistan's HSD supply chain business, by providing strategic infrastructure to transport HSD from Karachi to Shikarpur & Mahmoodkot. With the recent expansion, the company also started to supply MOGAS through the pipeline, which will eventually be reducing OMC's dependence on road transport, hence becoming the preferred choice for transporting HSD & MOGAS through WOP.

Revenues In line with the petroleum industry's performance, PAPCO throughput for 1HFY23 is approximately 2.2mln MT as compared to 1HFY22 was 2.2mln MT and capacity utilization increased to 58% (1HFY22: 50%, FY21: 45%) up by 8%. Henceforth, company's turnover for 1HFY23 clocked in at PKR 5.1bln (1HFY22: 3.8bln, 1HFY21 PKR 3.3bln). The company's topline is expected to improve through MOGAS revenue.

Margins During the period under review 1HFY23, overall margins of PAPCO remain stable, gross margins; 51.3% (1HFY22: 58.1%, 1HFY21: 63%). The bottom-line is largely supported by non-core income which is derived from short-term liquid investments. Net margins have recorded to be comparatively less than previous period: 1HFY23: 30.0%, 1HFY22: 47.2%, 1HFY21: 60.5%) owing to higher finance cost.

Sustainability In a bid for sustainable yet distinctive business model, PAPCO has introduced its much awaited MOGAS project. A value addition to company's present product portfolio. The delivery volumes are introduced to commence from FY22. The pipeline capacity to transport is 8mln tons of the commodity/annum, which can be increased to 12mln tons/annum, considered to be sufficient to meet the country's demand.

Financial Risk

Working Capital Working capital requirements of the company are dominated by payable days 1HFY23: 20 days (1HFY22: 13 days, 1HFY21: 31 days). As the storage tanks of PAPCO merely holds inventory for their customers, there exists small inventory holding period. Over the years PAPCO has negligible net working days. Net working capital requirements is fulfilled sufficiently by company's internal cash. Keeping in view of its requisites, there are no short-term borrowings for 1HFY23.

Coverages Company is able to generate sufficient free cashflows from operations; 1HFY23: PKR 2.6bln (FY22: PKR 6.02bln, FY21: 2.81bln). Interest coverage is mainly attributed to increased interest cost as compare to the FCFO due to increased policy rates and lesser throughput due to slow down in demand.

Capitalization PAPCO has aptly managed its capital structure in past years by keeping its leveraging in comfortable zone (1HFY23: 36%, 1HFY22: 40.7% & 1HFY21: 43.6%) However, from FY18 onward, leveraging took up an upwards pace (28.3%) and it witnessed a further hike during FY20. Foreign currency loan limit is USD 25mln from SCB-UK, which carry a mark-up rate of 3L+2.7%, payable in 12 equal instalments commencing from Dec21. The loan facility of PKR 11.8bln has been fully drawn down to date, which is exclusively obtained for the MOGAS project. Therefore, all the local and foreign loan has drawn down and repayments have been started to be made. Local currency loan is paid by PKR 4.6bln (As on Dec 31, 2022) and foreign currency loan is paid-off by PKR 10.5mln (As on Dec 31, 2022).



Pak Arab Pipeline Company Ltd. Pipeline Network	Dec-22 6M	Jun-22 12M	Jun-21 12M	Jun-20 12M
A BALANCE SHEET				
1 Non-Current Assets	22,662	22,829	21,651	21,588
2 Investments	16,914	17,984	14,864	16,308
3 Related Party Exposure	-	-	-	-
4 Current Assets	2,772	3,406	7,360	7,711
<i>a Inventories</i>	-	-	-	-
<i>b Trade Receivables</i>	1,296	555	336	435
5 Total Assets	42,348	44,218	43,875	45,607
6 Current Liabilities	8,849	8,455	8,219	8,738
<i>a Trade Payables</i>	994	136	221	704
7 Borrowings	10,498	11,888	13,609	15,532
8 Related Party Exposure	783	329	223	156
9 Non-Current Liabilities	2,225	2,255	1,312	1,299
10 Net Assets	19,993	21,290	20,512	19,882
11 Shareholders' Equity	19,993	21,290	20,512	19,882
B INCOME STATEMENT				
1 Sales	5,065	8,879	6,184	6,709
<i>a Cost of Good Sold</i>	(2,466)	(3,653)	(2,460)	(2,339)
2 Gross Profit	2,599	5,226	3,724	4,371
<i>a Operating Expenses</i>	(368)	(466)	(303)	(253)
3 Operating Profit	2,231	4,761	3,420	4,118
<i>a Non Operating Income or (Expense)</i>	780	2,358	1,659	1,678
4 Profit or (Loss) before Interest and Tax	3,011	7,119	5,079	5,795
<i>a Total Finance Cost</i>	(685)	(970)	26	9
<i>b Taxation</i>	(808)	(2,039)	(1,548)	(1,626)
6 Net Income Or (Loss)	1,519	4,110	3,557	4,178
C CASH FLOW STATEMENT				
<i>a Free Cash Flows from Operations (FCFO)</i>	2,570	6,017	2,811	3,421
<i>b Net Cash from Operating Activities before Working Capital Changes</i>	1,878	5,382	2,796	3,420
<i>c Changes in Working Capital</i>	1,023	4,558	(951)	368
1 Net Cash provided by Operating Activities	2,901	9,941	1,845	3,788
2 Net Cash (Used in) or Available From Investing Activities	1,545	(11,771)	8,107	(8,941)
3 Net Cash (Used in) or Available From Financing Activities	(4,486)	(5,637)	(10,848)	6,045
4 Net Cash generated or (Used) during the period	(40)	(7,467)	(897)	892
D RATIO ANALYSIS				
1 Performance				
<i>a Sales Growth (for the period)</i>	14.1%	43.6%	-7.8%	6.4%
<i>b Gross Profit Margin</i>	51.3%	58.9%	60.2%	65.1%
<i>c Net Profit Margin</i>	30.0%	46.3%	57.5%	62.3%
<i>d Cash Conversion Efficiency (FCFO adjusted for Working Capital/Sales)</i>	70.9%	119.1%	30.1%	56.5%
<i>e Return on Equity [Net Profit Margin * Asset Turnover * (Total Assets/Sl</i>	14.7%	19.7%	17.6%	22.0%
2 Working Capital Management				
<i>a Gross Working Capital (Average Days)</i>	33	18	23	26
<i>b Net Working Capital (Average Days)</i>	13	11	-5	-17
<i>c Current Ratio (Current Assets / Current Liabilities)</i>	0.3	0.4	0.9	0.9
3 Coverages				
<i>a EBITDA / Finance Cost</i>	4.7	10.0	475.9	N/A
<i>b FCFO / Finance Cost+CMLTB+Excess STB</i>	1.0	1.5	1.0	2.0
<i>c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)</i>	3.0	2.3	4.9	4.6
4 Capital Structure				
<i>a Total Borrowings / (Total Borrowings+Shareholders' Equity)</i>	36.1%	36.5%	40.3%	44.1%
<i>b Interest or Markup Payable (Days)</i>	12.3	22.2	977.0	N/A
<i>c Entity Average Borrowing Rate</i>	11.2%	5.0%	0.1%	0.0%

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.

Scale	Long-term Rating Definition
AAA	Highest credit quality. Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments
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.
AA-	
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.
A-	
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.
BBB	
BBB-	
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.
BB	
BB-	
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.
B-	
CCC	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.
CC	
C	
D	Obligations are currently in default.

Scale	Short-term Rating 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 conditions.
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 surveil 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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(1) Rating is just an opinion about the creditworthiness of the entity and does not constitute recommendation to buy, hold or sell any security of the entity rated or to buy, hold or sell the security rated, as the case may be | Chapter III; 14-3-(x)

2) Conflict of Interest

i. The Rating Team or any of their family members have no interest in this rating | Chapter III; 12-2-(j)

ii. PACRA, the analysts involved in the rating process and members of its rating committee, and their family members, do not have any conflict of interest relating to the rating done by them | Chapter III; 12-2-(e) & (k)

iii. The analyst is not a substantial shareholder of the customer being rated by PACRA [Annexure F; d-(ii)] Explanation: for the purpose of above clause, the term "family members" shall include only those family members who are dependent on the analyst and members of the rating committee

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(4) PACRA does not disclose or discuss with outside parties or make improper use of the non-public information which has come to its knowledge during business relationship with the customer | Chapter III; 10-7-(d)

(5) PACRA does not make proposals or recommendations regarding the activities of rated entities that could impact a credit rating of entity subject to rating | Chapter III; 10-7-(k)

Conduct of Business

(6) PACRA fulfills its obligations in a fair, efficient, transparent and ethical manner and renders high standards of services in performing its functions and obligations; | Chapter III; 11-A-(a)

(7) PACRA uses due care in preparation of this Rating Report. Our information has been obtained from sources we consider to be reliable but its accuracy or completeness is not guaranteed. PACRA does not, in every instance, independently verifies or validates information received in the rating process or in preparing this Rating Report | Clause 11-(A)(p).

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(9) PACRA ensures before commencement of the rating process that an analyst or employee has not had a recent employment or other significant business or personal relationship with the rated entity that may cause or may be perceived as causing a conflict of interest; | Chapter III; 11-A-(r)

(10) PACRA maintains principal of integrity in seeking rating business | Chapter III; 11-A-(u)

(11) PACRA promptly investigates, in the event of a misconduct or a breach of the policies, procedures and controls, and takes appropriate steps to rectify any weaknesses to prevent any recurrence along with suitable punitive action against the responsible employee(s) | Chapter III; 11-B-(m)

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(12) PACRA receives compensation from the entity being rated or any third party for the rating services it offers. The receipt of this compensation has no influence on PACRA's opinions or other analytical processes. In all instances, PACRA is committed to preserving the objectivity, integrity and independence of its ratings. Our relationship is governed by two distinct mandates i) rating mandate - signed with the entity being rated or issuer of the debt instrument, and fee mandate - signed with the payer, which can be different from the entity

(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)

(14) PACRA discloses that no shareholder directly or indirectly holding 10% or more of the share capital of PACRA also holds directly or indirectly 10% or more of the share capital of the entity which is subject to rating or the entity which issued the instrument subject to rating by PACRA; | Reference Chapter III; 12-2-(f)

(15) PACRA ensures that the rating assigned to an entity or instrument is 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 | Chapter III; 12-2-(i)

(16) PACRA ensures that the analysts or any of their family members shall not buy or sell or engage in any transaction in any security which falls in the analyst's area of primary analytical responsibility. This clause shall, however, not be applicable on investment in securities through collective investment schemes. | Chapter III; 12-2-(l)

(17) PACRA has established policies and procedure governing investments and trading in securities by its employees and for monitoring the same to prevent insider trading, market manipulation or any other market abuse | Chapter III; 11-B-(g)

Monitoring and review

(18) PACRA monitors all the outstanding ratings continuously and any potential change therein due to any event associated with the issuer, the security arrangement, the industry etc., is disseminated to the market, immediately and in effective manner, after appropriate consultation with the entity/issuer; | Chapter III | 18-(a)

(19) PACRA reviews all the outstanding ratings on semi-annual basis or as and when required by any creditor or upon the occurrence of such an event which requires to do so; | Chapter III | 18-(b)

(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 | 18-(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 | 18-(d)

Probability of Default

(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-(F-VII)

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