The Pakistan Credit Rating Agency Limited

Rating Report

Sitara Petroleum Service (Pvt.) Limited

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
11-May-2022	A-	A2	Stable	Maintain	-
19-May-2021	A-	A2	Stable	Maintain	-
19-May-2020	A-	A2	Stable	Maintain	-
15-Nov-2019	A-	A2	Stable	Maintain	-
16-May-2019	A-	A2	Stable	Initial	-

Rating Rationale and Key Rating Drivers

The Ratings reflect the sound business profile of Sitara Petroleum Service (Pvt) Ltd. ('Sitara Petroleum' or 'the Company') in line with current dynamics of petroleum industry. Sponsors of the Company are in the business for over three decades, reflecting their business acumen. The Company has exhibited improvement in margins on the back of high petroleum prices , lower operational costs and reduced financial costs. The financial risk profile is characterized by adequate leveraged capital structure. The equity has been boosted through profits. The Company has investment in real estate which supplement risk absorption capacity. The sponsors are engaged in real estate projects as well. The Company derives strategic impetus from its business ties with Gas & Oil Pakistan.

The ratings are dependent on the management's facility to sustain its business volumes while holding the margins. Sustaining the business and financial profile along with improvement in the governance framework would be vital for the ratings. Meanwhile, financial transparency is considered paramount.

Disclosure

Name of Rated Entity	Sitara Petroleum Service (Pvt.) Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology | Corporate Rating(Jun-21),Criteria | Correlation Between Long-term & Short-term Rating Scales(Jun-21),Criteria | Rating Modifiers(Jun-21)
Related Research	Sector Study | Oil Marketing Companies(Nov-21)
Rating Analysts	Behrooz Fareed | behrooz.fareed@pacra.com | +92-42-35869504

Profile

Legal Structure Sitara Petroleum Service (Pvt.) Limited (SPSL) is a private limited concern incorporated in July 2012.

Background Historically, there were two firms i) Lalpur Carriage: engaged in supplying logistics facility to Oil Marketing Companies (OMCs) & (ii) Sitara Petroleum engaged in selling and exporting POL goods through wholesale and direct sales. The management subsequently decided to give these organizations a proper structure under the umbrella of one organization i.e Sitara Petroleum (Pvt.) Limited

Operations SPSL is mainly engaged in the business of trading and distribution of Diesel, Petrol, and Lubricants. The Company is also providing fleet logistic services to OMCs in the country namely GO, PSO and Total PARCO. The Company is currently operating 42 fuel stations. The Company has petroleum storage capacity of 4.5 million liters and has carriage fleet of around 300 oil tankers. The registered office of the Company is situated at 14-T Gulberg-II, Lahore.

Ownership

Ownership Structure The Company is 94% owned by Mr. Tahir Iqbal, 4% by Mr. Muhammad Ali, while Mr. Muhammad Javed and Mr. Muhammad Hassan Javed own 1% each.

Stability The business has been governed and managed by seasoned individuals from the Oil sector of Pakistan. Sponsors are inducting next generation gradually into business, the succession planning however is not formally documented but implied.

Business Acumen The sponsor holds extensive experience and expertise in oil sector. Their strong business skills have helped the Company to achieve sustainable success over a period of years. Sponsors have Industry-specific working knowledge and strategic thinking capability.

Financial Strength Sponsors do not have any other business so financial strength is dependent on successful functioning of the SPSL.

Governance

Board Structure The Company has a seven-member board (including CEO). Board comprises two executives, two independent and 3 non-executive directors. Mr. Muhammad Ali has replaced Mr. Muhammad Akram as director of the company. Mr. Ali is the eldest son of Mr. Tahir Iqbal (CEO).

Members' Profile Mr. Muhammad Azmat is a seasoned businessman running leather tanneries for 20years and has significant experience in imports, exports, strategy and business management. Other Board members are also well qualified and have been associated with the Company for a reasonable period of time.

Board Effectiveness Roles of Chairman and CEO are performed by separate persons. Mr. Tahir Iqbal has been appointed as the CEO of SPSL and Mr. Azmat as Chairman. The board has two committees in place: (i) Audit Committee (ii) Human Resource & Remuneration Committee. The Board meets quarterly and meeting minutes are properly documented.

Financial Transparency The Company has appointed RSM Avais Hyder Liaquat Nauman Chartered Accountants. as its external auditor, listed in the "A" category on the State Bank of Pakistan's panel of auditors. They have expressed unqualified opinion on financial statements FY21.

Management

Organizational Structure A simplified organizational structure exists at the Company. The business profile segregated into four different departments, which are headed by their respective heads resulting in effective control and management. : (i) Operations, (ii) Finance, (iii) Sales, and (iv) Transport. All the heads report to CEO.

Management Team Mr. Tahir Iqbal is the CEO of SPSL, a veteran of the Retail & Oil Transportation sector with rich experience of more than 30 years. Mr. Shaheer Junaid is the CFO of the company, an EY alumni & Associate Chartered Accountant by profession and has over 6 years of professional experience in his portfolio. Most of the senior management is associated with the company since long and have sufficient experience to take strategic decisions.

Effectiveness SPSL has constituted two committees comprising members of the management team namely (i) Procurement and (ii) Retail Development Committee. The purpose of the Procurement Committee is to streamline the procurement process, establish effective controls and to ensure efficiency in procurement activities while Retail Development Committee ensures 'Retail Side' of the business is pursuing growth and precise strategies are being devised in the right direction.

MIS The Company uses ERP system based on Oracle RDBMS since January 2012. It runs various modules and generates reports as required. The IT infrastructure is effectively integrated with all the departments and ensures proper financial and operational control.

Control Environment The Company has an effective internal audit department which helps to improve risk management, control, and governance processes and brings improvement to business practices by forming SOPs.

Business Risk

Industry Dynamics The sector is highly regulated by OGRA, especially with respect to the prices of two major products, MOGAS and diesel. It was observed that global fuel prices have been escalating post pandemic, benefitting OMCs and distributors as they can pass on the hike to the consumers. However, record high prices can, in future, constrain the extent to which the changes in prices can be passed, should oil prices continue to follow an uptrend amid escalating geopolitical tensions in Eastern Europe. With the Pakistani economy recovering from the impacts of COVID-19, fuel demand has surged. It is expected that oil industry will continue to attain healthy margins, and will spike to pre-pandemic levels during FY22. During FY21, the sector's revenue registered a growth of 13.6%, owing to increased POL prices and volumetric sales. Additionally, three major products, HSD, MOGAS and RFO account for approximately 98% of the total POL consumption.

Relative Position During FY21, in the segment of trading and distribution of POL products, the Company has a considerable market share in PMG and HSD respectively, in the Punjab region. One of the key players in the industry, PAPCO, solely deals in High-Speed diesel transportation. However, in the near future, along with HSD, the company would be transporting MOGAS through an existing network. Because of this, relative positioning, in turn, the market share of the carriage companies will change.

Revenues During FY21, the Company witnessed a decrease of ~12% in total revenue from the corresponding period last year and reached to PKR~32,584mln (FY20 PKR~36,951mln) despite of increase in POL prices and better economic prospects as compared to corresponding period. This was majorly attributable to decreased sales volume. During 6MFY22, revenue of the Company stood at PKR~20,913mln).

Margins During FY21, Gross profit margins improved to ~4.8% despite decreased sales as the Company was able to benefit appreciation in inventory values and surge in POL prices (FY20: 4.1%). Owing to efficient deployment of resources Operating margins improved to ~4.5% during FY21 (FY20: 3.8~%). The effect of efficient management of operational expenses coupled with low finance cost trickled down to improved net profit margins to ~3% (FY20 ~2%). During 6MFY22, sales observed growth of 28% majorly attributable to increased POL prices and sales volume.

Sustainability Going forward, the Company intends to increase its retail outlet presence all over the cities of Pakistan, as well as in remote areas by installing more pumps. Additionally, the Company also aims to grow in the segment of Carriage Income by growing its number of fleets.

Financial Risk

Working Capital SPSL's working capital requirement emanates from its need to finance its trade debts and stock in trade. For this, the Company resorts to short-term borrowings. During FY21, the short-term financing of the Company surged by 2% (FY21: 3,760mln, FY20: PKR 3,551mln) due to stretched working capital. As at FY21, trade debts of the Company increased to ~4,423mln (FY20: PKR 1,881mln), trade payables to PKR~1,737mln (FY20: PKR~35mln) and inventory to PKR~855mln (FY20: PKR~371mln). SPSL is facing problems in managing its working capital which is evident from gross & net working capital days respectively. (FY21: 35 & 25 days; FY20: 19 & 18 days). During 2QFY22, working capital needs have remain stagnant.

Coverages Higher petroleum prices and better profitability during the period lead to higher FCFO (FY21: PKR ~2,028mln, FY20: PKR ~1,306mln). However, total finance cost decreased to (FY21: PKR ~356mln, FY20: PKR ~632mln) due to lower borrowings availed in this period and lower interest rate. Hence, interest coverage in FY21 stood at 5x from 2.6x in FY20). Core and total operating coverage improved to (FY21:2.8x FY20: 0.8x). Similarly, coverages improved during 2QFY22 to 2x.

Capitalization As at FY21, The Company has slightly leverage capital structure with debt-to-equity ratio of ~57%. The Company has total debt of PKR~ 4,846mln as FY21 and an equity of PKR ~3,707mln. However, capital structure has improved significantly to yield a debt-to-equity ratio of ~38% as at 2QFY22 due to significant decrease in short term borrowings.

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Financial Summary
PKR mln

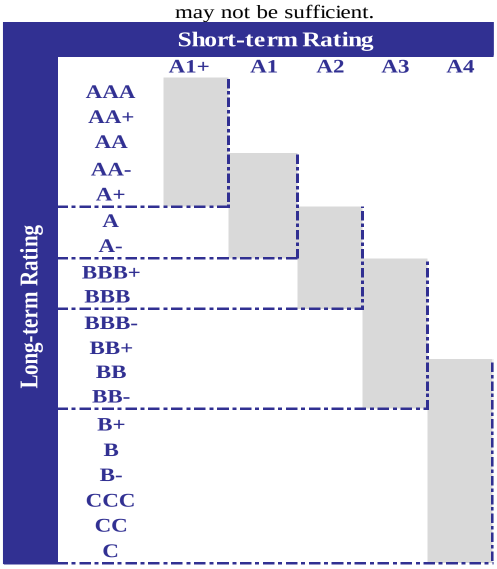
Sitara Petroleum (Pvt) Ltd.	Dec-21	Jun-21	Jun-20	Jun-19
OMC	6M	12M	12M	12M
A BALANCE SHEET				
1 Non-Current Assets	3,188	3,127	2,964	2,689
2 Investments	-	-	-	-
3 Related Party Exposure	577	1,305	1,838	550
4 Current Assets	4,551	6,288	3,046	4,867
a Inventories	*679*	*855*	*371*	*1,983*
b Trade Receivables	*3,468*	*4,423*	*1,881*	*1,887*
5 Total Assets	8,316	10,719	7,848	8,106
6 Current Liabilities	1,622	2,042	343	251
a Trade Payables	*1,445*	*1,737*	*35*	*29*
7 Borrowings	2,477	4,846	4,685	5,714
8 Related Party Exposure	-	-	-	-
9 Non-Current Liabilities	124	124	12	9
10 Net Assets	4,092	3,707	2,808	2,132
11 Shareholders' Equity	4,092	3,707	2,808	2,304
B INCOME STATEMENT				
1 Sales	20,913	32,584	36,951	27,873
a Cost of Good Sold	*(20,114)*	*(31,027)*	*(35,451)*	*(26,805)*
2 Gross Profit	799	1,557	1,499	1,068
a Operating Expenses	(59)	(96)	(86)	(118)
3 Operating Profit	740	1,462	1,413	950
a Non Operating Income or (Expense)	-	*174*	-	-
4 Profit or (Loss) before Interest and Tax	740	1,635	1,413	950
a Total Finance Cost	*(190)*	*(356)*	*(632)*	*(176)*
b Taxation	*(165)*	*(381)*	*(278)*	*(212)*
6 Net Income Or (Loss)	385	898	504	562
C CASH FLOW STATEMENT				
a Free Cash Flows from Operations (FCFO)	*658*	*1,336*	*1,305*	*923*
b Net Cash from Operating Activities before Working Capital Changes	*468*	*958*	*695*	*748*
c Changes in Working Capital	*1,887*	*(888)*	*465*	*(4,247)*
1 Net Cash provided by Operating Activities	2,356	70	1,160	(3,500)
2 Net Cash (Used in) or Available From Investing Activities	(144)	9	(381)	(336)
3 Net Cash (Used in) or Available From Financing Activities	(2,369)	(28)	(1,110)	3,985
4 Net Cash generated or (Used) during the period	(157)	50	(331)	149
D RATIO ANALYSIS				
1 Performance				
a Sales Growth (for the period)	28.4%	-11.8%	32.6%	--
b Gross Profit Margin	3.8%	4.8%	4.1%	3.8%
c Net Profit Margin	1.8%	2.8%	1.4%	2.0%
d Cash Conversion Efficiency (FCFO adjusted for Working Capital/Sales)	12.2%	1.4%	4.8%	-11.9%
*e Return on Equity [Net Profit Margin * Asset Turnover * (Total Assets/Sh*	19.8%	27.6%	19.7%	24.4%
2 Working Capital Management				
a Gross Working Capital (Average Days)	34	35	19	25
b Net Working Capital (Average Days)	21	25	18	24
c Current Ratio (Current Assets / Current Liabilities)	2.8	3.1	8.9	19.4
3 Coverages				
a EBITDA / Finance Cost	4.6	4.9	2.6	7.4
b FCFO / Finance Cost+CMLTB+Excess STB	2.0	1.9	0.7	1.2
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)	1.0	1.1	2.9	1.4
4 Capital Structure				
a Total Borrowings / (Total Borrowings+Shareholders' Equity)	37.7%	56.7%	62.5%	71.3%
b Interest or Markup Payable (Days)	0.0	0.0	13.1	0.0
c Entity Average Borrowing Rate	10.6%	8.1%	11.8%	2.7%

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):

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

Instruments
a) Basel III Compliant Debt Instrument Rating
b) Debt Instrument Rating
c) Sukuk Rating

Regulatory and Supplementary Disclosure
(Credit Rating Companies Regulations,2016)

Rating Team Statements
(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

Restrictions
(3) No director, officer or employee of PACRA communicates the information, acquired by him for use for rating purposes, to any other person except where required under law to do so. | Chapter III; 10-(5)
(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.
(8) PACRA prohibits its employees and analysts from soliciting money, gifts or favors from anyone with whom PACRA conducts business | Chapter III; 11-A-(q)
(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)

Independence & Conflict of interest
(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)
Proprietary Information