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
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 vigorous business profile of Sitara Petroleum Service (Pvt.) Limited. Sponsors have been engaged in the business for over three decades, reflecting their business acumen. Sitara operates a network of ~40 retail stations which are mainly spread out in the Central and Southern Punjab region while providing POL products directly to customers in bulk. The company is engaged in fleet logistic accommodations (Carriage Income) to OMCs (mainly to Gas & Oil Pakistan Ltd). The sponsor's long association with these business lines is being considered positive. The company's prime profits are being engendered by the fleet logistics business. It carries ~68% share in the gross profit, followed by retail (~22%) and bulk business segments (~10%). The income from the fleet logistics division has soared over the years as the fleet size expands whereas retail and bulk segments supplement the profitability. The financial risk profile is characterized by an adequate leveraged capital structure. The equity has been boosted through profits. The company has sizable land holdings, which supplemet risk absorption capacity. The sponsors are engaged in real estate projects; these have been partly financed through group companies including Sitara Petroleum. The related and ensuing risk must be adequately managed.

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 Ratings(Jun-20),Methodology | Correlation Between Long-Term And Short-Term Rating Scale(Jun-20),Criteria | Rating Modifier(Jun-20)
Related Research	Sector Study | Oil Marketing Companies(Nov-20)
Rating Analysts	Faraan Taimoor | faraan.taimoor@pacra.com | +92-42-35869504

Profile

Legal Structure Sitara Petroleum Service (Pvt.) Limited was incorporated in July 2012. The Head Office of the company is situated at Tufail Shaheed Road near PSO Depot, Sahiwal.

Background Historically, there were two firms i) Lalpur Carriage: engaged in supplying logistics facility to Oil Marketing Companies (OMCs) & (ii) Sitara Petroleum: engaged in the sector of 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 Sitara Petroleum Service (Pvt) Limited is mainly engaged in the business of trading and distribution of Diesel, Petrol, and Lubricants. The company is also providing fleet logistic services (Carriage Income) to OMCs in the country namely GO, PSO and Total PARCO.

Ownership

Ownership Structure The company is 94% owned by Mr. Tahir Iqbal, 4% by Mr. Muhammad Akram, 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. Mr. Khalid Riaz, brother of Mr. Tahir Iqbal, has no direct ownership in Sitara, however, he bears stronghold in the strategic decision making of the company, in case the company needs it. Though ownership of the company is clearly defined, the succession planning however is not well-documented.

Business Acumen Sitara's sponsors have strong business skills which 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 financial strength is subject to the successful functioning of the Sitara Petroleum Service (Pvt) Limited.

Governance

Board Structure The company has a seven-member board (including CEO). Board comprises two executives, two independent and 3 non-executive directors.

Members' Profile The BoD has diversified experience and knowledge of the industry which is considered good.

Board Effectiveness The company has separated the roles of Chairman and CEO. Mr. Tahir Iqbal has been appointed as the CEO of Sitara Petroleum (Pvt) Ltd and Mr. Muhammad Akram has been assigned the post of Chairman of the Board. The board has two committees in place: i) Audit Committee and ii) Human Resource & Remuneration Committee.

Financial Transparency The auditors of the company are RSM Avais Hyder Liaquat Nauman performing the Annual Audit Exercise for the Fiscal Year Ended June'20. The firm is rated A in the State Bank of Pakistan's list of auditors.

Management

Organizational Structure The company has an adequate organizational structure. The operations of the company have been bifurcated into four broad functional areas which comprise: i) Operations, ii) Finance, iii) Sales, and iv) Transport.

Management Team Mr. Tahir Iqbal is the CEO of Sitara Petroleum Service (Pvt.) Ltd. He is a veteran of the Retail & Oil Transportation sector with rich experience in the field spanning more than 30 years. Mr. Shaheer Junaid is the CFO of the company, an 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 contribute and take strategic decisions.

Effectiveness Sitara has constituted two committees comprising members of the management team namely i) Procurement and ii) Retail Development Committee.

MIS The Company uses ERP Software designed & developed by Vision Plus. It is developed by using Oracle RDBMS. It has a variety of information analysis and various modules including General Ledger, Sales & Receivables, Purchase & Payables, Inventory Control, Carriage & Freight, and Transport & Monitoring.

Control Environment The company is using a fleet management system to keep a track on the movement of Tank Lorries and Vehicles on the move. This is done through the tracker system. A special structure is designed in the system to track all the trips that are system logged. Sitara has internal audit department which adds value and improvement to the organization's control environment.

Business Risk

Industry Dynamics Industry Dynamics Pakistan consumed a total of ~19.3mln (MT) of POL products in FY20 (FY19: 25.1mln MT), ~23% lower than the same period last year. This decline is seen mainly owing to a decrease in the sales of Furnace oil by ~51% to ~3.5mln MT (FY19: ~7.5mln MT), as the government of Pakistan plans to gradually reduce reliance on oil-based power plants to other power sources i.e. LNG & coal. MOGAS, FO, and HSD are three major products that are widely used because of their immense consumption in the country.

Relative Position During FY20, 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 Topline of the company can be bifurcated into i) POL Retail Sales ii) POL Bulk Sales and iii) Carriage Income. During 9MFY21, retail sales yielded 59% in the total revenue mix, while Bulk Sale and Carriage Income contribute ~26% and ~15% respectively. During 9MFY21, total sales of the company stood at ~PKR 26bln (FY20: PKR 37bln).

Margins During 9MFY21, the company's profits were being generated from the transportation business. This carries a ~68 % share in the gross profit, followed by ~35% in retail and ~14% in the bulk segment. Over the years, the share of profit from the fleet logistics division is soaring while retail and bulk segments are also rising. In most segments, Sitara's margins are regulated not negotiated. During 9FY21, the total gross profit of the company stood at ~PKR 1.1bln (FY20: ~PKR1.5bln).

Sustainability Going forward, Sitara 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. Management, being cognizant of the current industry situation is embarking on functionalizing an Oil Marketing Company to augment and diversify its revenue stream, in addition to current business. The company's venture into OMC segment has been put on hold.

Financial Risk

Working Capital Sitara'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 9MFY21, the short-term financing of the company dropped by an enormous ~47% (9MFY21: 1,860mln, FY20: PKR 3,551mln). Trade debts of the company as at 9MFY21 remained stable at PKR 1,716mln (FY20: PKR 1,887mln). The company has been managing its working capital requirements efficiently which is evident from its gross working capital cycle days (9MFY21: 24, FY20: 30, FY19: 29 days).

Coverages During 9MFY21, the company has generated cash flow (FCFO) of PKR 926mln (FY20: PKR 1,305mln, FY19: PKR 923mln).

Capitalization The company's long-term loan consists of demand finance and lease finance. These loans were obtained for the acquisition of commercial vehicles and the renovation of petrol pumps. Sitara has a leveraged capital structure at 9MFY21 of 47% (FY20: 61%, FY19: 71%). This decrease was on account of the repayment of lease and the partial settlement of short-term debt. The company has buffered up its equity through bonus shares.

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Sitara Petroleum (Pvt.) Limited	**Mar-21**	**Jun-20**	**Jun-19**
OMC	**9M**	**12M**	**12M**
A BALANCE SHEET			
1 Non-Current Assets	3,769	2,964	2,689
2 Investments	-	-	-
3 Related Party Exposure	638	1,838	550
4 Current Assets	2,672	3,046	5,039
a Inventories	*466*	*371*	*1,983*
b Trade Receivables	*1,716*	*1,881*	*1,887*
5 Total Assets	7,078	7,848	8,278
6 Current Liabilities	963	343	251
a Trade Payables	*748*	*33*	*29*
7 Borrowings	2,833	4,685	5,714
8 Related Party Exposure	-	-	-
9 Non-Current Liabilities	12	12	9
10 Net Assets	3,270	2,808	2,304
11 Shareholders' Equity	3,270	2,808	2,304
B INCOME STATEMENT			
1 Sales	25,677	36,951	27,873
a Cost of Good Sold	*(24,624)*	*(35,451)*	*(26,805)*
2 Gross Profit	1,052	1,499	1,068
a Operating Expenses	(73)	(86)	(118)
3 Operating Profit	980	1,413	950
a Non Operating Income or (Expense)	-	-	-
4 Profit or (Loss) before Interest and Tax	980	1,413	950
a Total Finance Cost	*(313)*	*(632)*	*(176)*
b Taxation	*(204)*	*(278)*	*(212)*
6 Net Income Or (Loss)	462	504	562
C CASH FLOW STATEMENT			
a Free Cash Flows from Operations (FCFO)	*926*	*1,305*	*923*
b Net Cash from Operating Activities before Working Capital	*601*	*695*	*748*
c Changes in Working Capital	*2,207*	*465*	*(4,247)*
1 Net Cash provided by Operating Activities	2,809	1,160	(3,500)
2 Net Cash (Used in) or Available From Investing Activities	(955)	(381)	(336)
3 Net Cash (Used in) or Available From Financing Activities	(1,852)	(1,110)	3,985
4 Net Cash generated or (Used) during the period	2	(331)	149
D RATIO ANALYSIS			
1 Performance			
a Sales Growth (for the period)	-7.3%	32.6%	4.7%
b Gross Profit Margin	4.1%	4.1%	3.8%
c Net Profit Margin	1.8%	1.4%	2.0%
d Cash Conversion Efficiency (FCFO adjusted for Working Ca	12.2%	4.8%	-11.9%
*e Return on Equity [Net Profit Margin * Asset Turnover * (To*	17.9%	17.5%	33.8%
2 Working Capital Management			
a Gross Working Capital (Average Days)	24	30	29
b Net Working Capital (Average Days)	19	30	29
c Current Ratio (Current Assets / Current Liabilities)	2.8	8.9	20.1
3 Coverages			
a EBITDA / Finance Cost	3.6	2.5	6.4
b FCFO / Finance Cost+CMLTB+Excess STB	1.6	0.7	1.6
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Fin	1.4	2.9	1.2
4 Capital Structure			
a Total Borrowings / (Total Borrowings+Shareholders' Equity	46.4%	62.5%	71.3%
b Interest or Markup Payable (Days)	9.2	12.8	0.0
c Entity Average Borrowing Rate	11.1%	12.2%	4.7%

#	Notes
	All figures in PKR mln (excluding D Ratio Anlysis)

Credit Rating

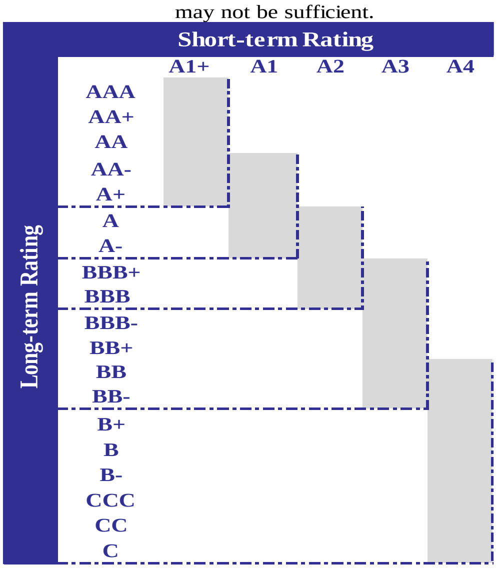
Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

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

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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

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(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)
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(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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