The Pakistan Credit Rating Agency Limited

Rating Report

National Refinery Limited

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
27-May-2022	AA+	A1+	Negative	Maintain	-
28-May-2021	AA+	A1+	Negative	Maintain	-
30-May-2020	AA+	A1+	Negative	Maintain	-
29-Nov-2019	AA+	A1+	Stable	Maintain	-
31-May-2019	AA+	A1+	Stable	Maintain	-
07-Dec-2018	AA+	A1+	Stable	Maintain	-
30-May-2018	AA+	A1+	Stable	Maintain	-
23-Jun-2017	AA+	A1+	Stable	Maintain	-
22-Sep-2016	AA+	A1+	Stable	Maintain	-

Rating Rationale and Key Rating Drivers

The ratings reflect National Refinery Limited's (NRL) association with the integrated oil group – Attock Group (AG). The strength of the Company is its base oil business wherein NRL possesses a notable share in meeting the economy's demand for lubricants. Global recovery has been witnessed in the oil demand leading to higher volumetric sales coupled with higher pricing of petroleum products, leading to better GRMs and profitability margins for the local refinery sector. However, uncertainty still prevails with respect to oil supplies as a result of Russia-Ukraine conflict which could further impact the pricing dynamics. NRL's core business remains exposed to the vicissitudes in international crude and petroleum products' (POL) prices, which in turn, steer the gross refining margins (GRMs) of the Company. Throughput of fuel refinery operations declined to 61% as compared to 67% in the corresponding period mainly due to planned turnaround of fuel refinery however, this decrease is offset by the lube segment where throughput improved to 86% as compared to 79% during same period last year. During the period ended March 31, 2022, the Company's profitability improved after reporting a net profit of PKR 3,673mln (9MFY21: PKR 892mln). Sales have improved majorly on the back of increase in international oil prices and better volumes especially in lube segments. Upward revision in policy rate and decline in Pak Rupee against US Dollar during the period impacted the NRL's profitability. The working capital requirement of the Company have also increased considerably due to sharp increase in crude oil prices.

The local refinery sector is going through some significant challenges pertaining to up-gradation of the refining complex. The company along with other refineries has been in continuous discussion with the government to finalize a refinery policy that would address the upgradation concerns along with certain fiscal and tariff concessions to the refining sector. However, no final approval has been granted by the government which is expected to get delayed further amid current political instability in the country. The ratings are dependent upon NRL's ability to effectively shield its business profile from external vulnerabilities. Revived performance indicators and prudent financial matrix are imperative to uphold the ratings. Further outlook of the Company is expected to improve as the company is projected to recover from the losses incurred previously during the lockdown period on account of sustainability in international oil prices and available demand drivers in the market. Further, the approval of proposed Refining Policy, which will enhance Refineries' ability to upgrade remains imperative for the ratings.

Disclosure

Name of Rated Entity	National Refinery 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 | Refineries(Nov-21)
Rating Analysts	Anam Waqas Ghayour | anam.waqas@pacra.com | +92-42-35869504

Profile

Legal Structure National Refinery Limited (NRL), is listed on the Pakistan Stock Exchange, since the year 1964. The Government of Pakistan took over the management of NRL as per the Economic Reforms Order, 1972 under the Ministry of Production, which exercised control through its shareholding in State Petroleum Refining and Petrochemical Corporation (PERAC).

Background In June 2003, the Government of Pakistan decided to include NRL in its privatization program. The sale of 51% equity and transfer of management control to a strategic investor was proposed accordingly. After competitive bidding, NRL was acquired by the Attock Group (AG) in July 2005.

Operations NRL is engaged in the manufacturing, production, and sale of a large range of petroleum products. The refinery complex of the company comprises three refineries, consisting of two lube refineries and one fuel refinery.

Ownership

Ownership Structure Attock Group retains the majority stake (51%), through Attock refinery limited (25%), its Group Company Pakistan Oilfields Limited (POL) (25%) and Attock Petroleum Limited (APL) (1%). Other major shareholders include; Islamic Development Bank (~15%), Institutions collectively include Banks, Insurance Companies, NBFIs, Joint Stock Companies, Investment Companies, Modarabas, Mutual Funds and Trusts etc. holds (~18%). The general public holds ~16% of the shareholding.

Stability The Group is governed and administered by Attock Group (AG), a distinguished name in the oil sector of Pakistan.

Business Acumen The Pharaon Group is the principal stakeholder of AG and is engaged internationally in diversified activities, which include hotels, oil exploration, production and refining, chemicals, cement, and real estate.

Financial Strength NRL is a member of a conglomerate which is a fully integrated group covering all segments of oil and gas industry from exploration, production, and refining, to marketing of a wide range of petroleum products.

Governance

Board Structure The Company has a eight member board of directors including five Non-Executive Directors, two Independent Directors and one Executive Director. There are five representatives of the AG. The Independent directors include one nominee representing Islamic Development Bank.

Members' Profile Mr. Shuaib A. Malik, was appointed as a chairman of the board after serving several years as deputy chairman & chief executive officer. He has been associated with Attock Group for about 45 years and is a veteran of the oil business. The remaining board members have significant relevant experience and expertise in the oil industry.

Board Effectiveness The board conducts regular meetings every quarter to discuss the operational and financial performance of the refinery. Furthermore, the board has constituted two committees to maintain effective oversight and efficient functioning. These comprise; a) Audit Committee and b) HR & Remuneration Committee.

Financial Transparency NRL's auditors, A. F. Ferguson & Co Chartered Accountants, a member firm of the PwC network, expressed an unqualified opinion on the company's financial statements for FY21. The State Bank of Pakistan categorizes the firm, in the A category of auditing firms.

Management

Organizational Structure The company primarily operates through four divisions namely: a) Operations, b) HR & Admin c) Commercial and Procurement, and d) Finance & Corporate Affairs. The special project division is temporally established to work on major projects. All divisional heads report to the CEO.

Management Team The CEO, Mr. Jamil A. Khan, has been associated with the company since 2005. He has been serving as the chief executive officer from Nov'18. Mr. Nouman Ahmed Usmani is the CFO of the company, who has been associated with NRL, for ~13 years. He is well qualified and brings an overall experience of ~21 years with him. The senior management is accompanied by a team of qualified and experienced individuals.

Effectiveness The company has an Executive Committee in place, comprising the CEO along with the General Manager Commercial and Procurement. The committee meets on a need basis and ensures smooth refinery operations as well as formulating new strategies to deal with developments in the refinery sector.

MIS MIS presented to the board is strong and shared on a quarterly basis. NRL has employed ERP ECC-6, developed by SAP. The company generates MIS reports on a daily, fortnightly and monthly basis. These mainly include daily cash position, daily production report, saleable stock position, treasury and accounts section MIS, debtors aging, monthly management accounts, quarterly budget and expense reporting. Some reports are generated in excel format, as well.

Control Environment NRL has developed an in-house system – Crude Oil Management System for recording functions pertaining to oil movements and purchases of crude oil. NRL uses in-house reports in balancing crude oil inventory. Meanwhile, the company has established a Disaster Recovery Site equipped with the latest technology ensuring smooth functionality in case of a natural disaster.

Business Risk

Industry Dynamics The country consumed a total of ~16.5mln metric tons (MT) of refined petroleum products in 9MFY22 (FY21: ~19.8mln MT). During this period the global prices of crude oil and petroleum products remained volatile. However, gradual recovery has been witnessed in overall oil demand after the easing of Covid. Going forward, the demand/supply and pricing of crude oil and petroleum products is expected to remain unstable due to the geo political situation and local political instability.

Relative Position With respect to the relative positioning of the players in the premium products (HSD and MOGAS); efficiency and utilization of available capacity is essential. Based on Net Sales for the nine month period ending March 2022, PARCO holds the majority market share of 48% while Cnergyico and Pakistan Refinery hold 11% each. Attock Refinery contributes 16% while National Refinery contributes 15% to the total domestic supply of POL products.

Revenues An upward trend in the turnover was noted, with the net revenue amounting to PKR~154,254mln during 9MFY22 (FY21: PKR~139,625mln), due to improved sales volume and increased global oil prices after a positive shift was witnessed in the recovery of local demand for petroleum products. During the period the company earned profit after tax of PKR 3,673mln resulting from the better performance in the Lube segment that generated a profit after tax of PKR 3,890mln (9MFY21: PKR 2,666mln).

Margins Net profit margins turned positive in period under review 9MFY22, standing at 2.4% (FY21: 1.3%). As a result of rising petroleum prices, similar trend was noticed in Gross Profit Margins clocking in at 5.7% during 9MFY22 (FY21: 2.8%).

Sustainability The refinery sector has been witnessing a downfall in demand post Covid. During the period under review, the demand for petroleum products increased leading to recovering gross refinery margins. Although, the prices of crude oil and petroleum products remain uncertain in the global market, during the period the local market experienced better pricing. Going forward, the upgradation of the refinery is crucial for its sustainability, for which the company and other refineries are in deliberations with the Government to draft a refinery policy for sustenance of the overall sector.

Financial Risk

Working Capital NRL's working capital requirement emanates from import of raw materials and remains a function of fluctuating crude oil prices in international markets. During the period the local refinery sector witnessed a recovering trend in the demand of petroleum products. NRL's average gross working capital days during 9MFY22, remained somewhat similar at 68 days (FY21: 60 days). The same trend was noted in the average net working capital days (9MFY22: 37 days, FY21: 28 days.

Coverages Free Cash Flows from Operations (FCFO) during 9MFY22 amounted to PKR ~6,766mln (FY21: PKR ~6,359mln). FCFO turned positive after FY20, owing to the improved profitability resulting increased sales volume and improved prices. Consequently, the coverages show and improving trend with the ratio FCFO-to-Finance Cost, clocking in at 3.3x (FY21: 4.0x).

Capitalization The debt-to-equity ratio, as at 9MFY22, clocked in at 51.9% (FY21: 39.0%), depicting a highly leveraged structure. Short-term loans constitute 100% of the total borrowings in order to meet working capital needs.

The Pakistan Credit Rating Agency Limited

Financial Summary
PKR mln

National Refinery Limited	Mar-22	Jun-21	Jun-20	Jun-19
Refineries	9M	12M	12M	12M
A BALANCE SHEET				
1 Non-Current Assets	37,604	39,480	41,954	38,665
2 Investments	10	10	13	13
3 Related Party Exposure	-	-	-	-
4 Current Assets	56,598	36,192	21,346	37,489
a Inventories	*33,456*	*21,404*	*11,820*	*25,669*
b Trade Receivables	*12,582*	*9,032*	*4,022*	*7,499*
5 Total Assets	94,212	75,682	63,313	76,168
6 Current Liabilities	21,697	22,916	16,202	16,994
a Trade Payables	*17,495*	*17,134*	*7,843*	*10,290*
7 Borrowings	37,164	20,181	16,965	25,008
8 Related Party Exposure	-	-	-	-
9 Non-Current Liabilities	890	997	309	293
10 Net Assets	34,460	31,587	29,837	33,873
11 Shareholders' Equity	34,460	31,587	29,837	33,873
B INCOME STATEMENT				
1 Sales	154,254	139,625	125,613	160,906
a Cost of Good Sold	*(145,405)*	*(135,700)*	*(136,730)*	*(165,355)*
2 Gross Profit	8,850	3,925	(11,118)	(4,449)
a Operating Expenses	(1,757)	(1,823)	(1,598)	(1,646)
3 Operating Profit	7,093	2,101	(12,716)	(6,095)
a Non Operating Income or (Expense)	*(2,626)*	*903*	*97*	*(3,735)*
4 Profit or (Loss) before Interest and Tax	4,467	3,005	(12,619)	(9,830)
a Total Finance Cost	*(2,076)*	*(1,604)*	*(2,244)*	*(1,199)*
b Taxation	*1,282*	*370*	*10,799*	*2,337*
6 Net Income Or (Loss)	3,673	1,770	(4,064)	(8,692)
C CASH FLOW STATEMENT				
a Free Cash Flows from Operations (FCFO)	*6,766*	*6,359*	*(5,274)*	*(5,185)*
b Net Cash from Operating Activities before Working Capital Changes	*5,166*	*4,575*	*(7,539)*	*(6,001)*
c Changes in Working Capital	*(20,324)*	*(7,314)*	*17,219*	*(14,828)*
1 Net Cash provided by Operating Activities	(15,157)	(2,739)	9,680	(20,830)
2 Net Cash (Used in) or Available From Investing Activities	(426)	(395)	(1,844)	(1,517)
3 Net Cash (Used in) or Available From Financing Activities	16,169	3,189	(8,262)	22,783
4 Net Cash generated or (Used) during the period	586	55	(426)	437
D RATIO ANALYSIS				
1 Performance				
a Sales Growth (for the period)	47.3%	11.2%	-21.9%	17.5%
b Gross Profit Margin	5.7%	2.8%	-8.9%	-2.8%
c Net Profit Margin	2.4%	1.3%	-3.2%	-5.4%
d Cash Conversion Efficiency (FCFO adjusted for Working Capital/Sales)	-8.8%	-0.7%	9.5%	-12.4%
*e Return on Equity [Net Profit Margin * Asset Turnover * (Total Assets/Shareholders' Equity)]*	15.8%	6.1%	-12.4%	-27.5%
2 Working Capital Management				
a Gross Working Capital (Average Days)	68	60	71	61
b Net Working Capital (Average Days)	37	28	45	34
c Current Ratio (Current Assets / Current Liabilities)	2.6	1.6	1.3	2.2
3 Coverages				
a EBITDA / Finance Cost	3.4	4.1	-4.0	-5.2
b FCFO / Finance Cost+CMLTB+Excess STB	1.9	0.8	-0.4	-0.9
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)	0.4	1.4	-1.6	-0.7
4 Capital Structure				
a Total Borrowings / (Total Borrowings+Shareholders' Equity)	51.9%	39.0%	36.2%	42.5%
b Interest or Markup Payable (Days)	71.8	21.7	50.6	111.1
c Entity Average Borrowing Rate	9.7%	7.9%	11.0%	11.2%

Credit Rating

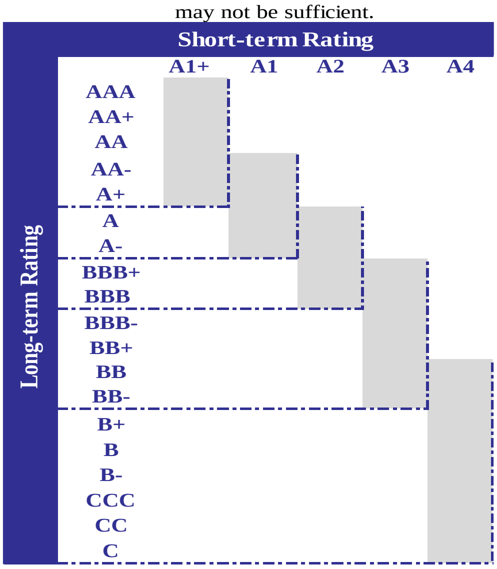
Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

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