RATING REPORT

Pakistan State Oil Company Limited

REPORT DATE:
December 12, 2024
RATING ANALYSTS:
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RATING DETAILS				
Rating Category	**Latest Rating**		**Previous Rating**	
	Long-term	**Short-term**	**Long-term**	**Short-term**
Entity	AA+	A1+	AA+	A1+
Rating Date	*December 12, 2024*		*January 19, 2024*	
Rating Outlook/Watch	Reaffirmed		Reaffirmed	
Rating Action	*Stable*		*Stable*	

COMPANY INFORMATION

Incorporated in 1976	External auditors: **KPMG Taseer Hadi & Co.**
Listed Public Limited Company	**Chairman of the Board:** Asif Baigmohamed
Key Shareholders (with stake 5% or more): Government of Pakistan (direct and indirect) – **51%**	**Managing Director & Chief Executive Officer:** Syed Muhammad Taha

APPLICABLE METHODOLOGY(IES)

VIS Entity Rating Criteria Methodology – Industrial Corporates & Government Supported Entities
https://docs.vis.com.pk/docs/CorporateMethodology.pdf
https://docs.vis.com.pk/docs/Meth-GSEs202007.pdf

APPLICABLE RATING SCALE(S)

VIS Issue/Issuer Rating Scale:
https://docs.vis.com.pk/docs/VISRatingScales.pdf

Pakistan State Oil Company Limited

OVERVIEW OF THE INSTITUTION	RATING RATIONALE

Pakistan State Oil Company Limited (PSO) is a public company incorporated in Pakistan in 1976 and is listed on the Pakistan Stock Exchange Limited. The registered office of the company is located in Karachi. Principal activities of the company are procurement, storage and marketing of petroleum and related products. It also blends and markets various kinds of lubricating oils.

Profile of Chairman

Mr. Asif Baigmohamed became the Chairman of PSO in May 2023. He is the Group Chief Executive Officer of Baigmohamed Group of Companies and CEO of ABM Investment, a private equity firm. Mr. Baigmohamed is a graduate of Brown University.

Profile of Managing Director & CEO

Syed Muhammad Taha possesses over 3 decades of cross industry experience. Previously, he worked at Oasis Energy and K-Electric Limited. Mr. Taha has also worked for almost a decade at PSO. Mr. Taha holds an Engineering degree, with an MBA in Finance from the Institute of Business Administration Karachi.

Company Profile

Pakistan State Oil Company Limited ("PSO" or "the Company") is a public company incorporated in Pakistan in 1976 and is listed on the Pakistan Stock Exchange Limited. It is the country's largest oil marketing company (OMC). The principal activities of the Company are procurement, storage and marketing of petroleum and related products. It also blends and markets various kinds of lubricating oils.

The registered office of the Company is located at PSO House, Khayaban-e- Iqbal, Clifton, Karachi. The business units of the Company include the following:

- Head Office - PSO House, Khayaban-e-Iqbal, Clifton, Karachi.
- Lubes Manufacturing Plant - National Refinery Limited, Korangi, Karachi. Kemari Oil Terminal, Kemari, Karachi.

The Government of Pakistan (GoP) holds a controlling interest of ~51% in PSO, with management oversight through both direct and indirect ownership. The GoP has full authority to appoint the Board of Management and the Managing Director. In addition, PSO has strategic stakes in several companies, including Asia Petroleum Limited (49%), Pak Grease Manufacturing Company Limited (22%), Pakistan Refinery Limited (PRL) (63.56%), and Pak-Arab Pipeline Company Limited (PAPCO) (12%). PSO also owns subsidiaries, namely Cerisma (Private) Limited, PSO Renewable Energy (Private) Limited, and PSO Venture Capital (Private) Limited. As a result, PSO's vertically integrated supply chain infrastructure is crucial to its business operations and overall market risk management.

Operational Highlights:

PSO's products are segregated into the following three categories

a) White oils – comprising high speed diesel (HSD), motor gasoline (MS), jet petroleum (JP-1), and kerosene oil (SKO),

b) Black oils – comprising furnace oil (FO), and light diesel oil (LDO), and

c) Lubricants and chemicals.

PSO has streamlined operations by re-engineering & digitizing 760 processes into a more efficient 430 processes. Additionally, the Company is targeting the integration of Artificial Intelligence across all operations to elevate people's capabilities and operational efficiency. During FY24, PSO added 101 retail outlets, increasing the total to 3,580. It also rehabilitated 48,000 tons of storage while 91,000 tons of new storage were also added, bumping total storage capacity to 1.24m tons. In September 2024, PSO successfully signed a long-term LPG Supply Agreement (SPA) with United Energy Pakistan Ltd. (UEP), resulting in a 25% increase in its LPG allocation. These initiatives are part of PSO's efforts to strengthen its infrastructure and enhance operational capacity.

PSO's subsidiaries are incorporated in Karachi, contributing to various sectors with distinct business models. Pakistan Refinery Limited (PRL) has leveraged the brownfield refining policy, with the front-end-engineering-design (FEED) completion slated for December 2024, marking progress in its strategic growth trajectory. A key milestone achieved by fintech Cerisma (Pvt.) Limited is the in-principal approval for an EMI license, laying the groundwork for an advanced digital financial infrastructure. In parallel, PSO Renewable Energy (Pvt.) Limited is driving sustainability through establishing solar initiatives across various sectors. Furthermore, PSO Venture Capital (Pvt) Limited has expanded its investment portfolio by venturing into fund management by focusing on nurturing innovative start-ups.

Industry Review

In FY24, Pakistan's oil marketing sector faced significant challenges, marked by a notable decline in petroleum product sales. Total sales dropped by 8% year-on-year (YoY) to 15.28 million tons, the lowest since FY06. This downturn was attributed to economic pressures, elevated fuel prices, and competition from smuggled fuel. Despite these challenges, June 2024 saw a temporary recovery, with sales reaching 1.45 million tons, the highest in 19 months, primarily due to reductions in petrol and diesel prices. However, the overall annual performance remained subdued, reflecting the sector's struggle to maintain momentum amid economic headwinds.

Conversely, the lubricant industry demonstrated resilience during FY24. Despite facing inflation, import restrictions, and a downturn in automotive sales, the sector achieved 3% growth. PSO notably outperformed the market, recording a 9.7% increase in lubricant sales and capturing a 26.9% market share, a 1.6% rise from the previous year. However, smaller players in the market continued to struggle during the period.

Key Rating Drivers

Business Risk Profile

Sector Risk; Oil Marketing Companies: High

The business risk profile for the OMC sector in Pakistan is assessed as High, reflecting exposure to regulatory oversight, market competition, and macroeconomic volatility. The sector operates in a regulated environment, with pricing and profit margins governed by government policies. Additionally, challenges stemming from currency depreciation, liquidity constraints, and fluctuations in international oil prices elevate the risk profile.

The sector's operational dynamics are shaped by the import-dependent nature of fuel products, exposing OMCs to exchange rate risks – mitigated to an extent by the pricing mechanism by the government - and delays in payments under the government's pricing and subsidy mechanisms. Moreover, competition among OMCs in terms of infrastructure investments and market share requires significant capital outlay, which can strain financial flexibility.

Sector Risk; Lubricants: Medium

The business risk profile for Pakistan's lubricant sector is assessed as medium, influenced by stable demand drivers, competitive market dynamics, and exposure to economic fluctuations. The sector benefits from consistent demand across automotive and industrial applications; however, it faces challenges related to raw material costs, currency volatility, and regulatory considerations.

Demand for lubricants is closely linked to the performance of the automotive and industrial sectors. While the automotive industry has shown growth, economic uncertainties and inflationary pressures may affect vehicle sales and, consequently, lubricant consumption. Industrial demand remains steady, though it is susceptible to broader economic conditions.

The market is characterized by the presence of both multinational corporations and local manufacturers, leading to competitive pricing and innovation pressures. Additionally, the prevalence of counterfeit products poses reputational risks and impacts market share for legitimate producers.

The sector relies heavily on imported base oils and additives, making it vulnerable to exchange rate fluctuations and global supply chain disruptions. Regulatory policies, including environmental standards and taxation, also play a significant role in shaping operational frameworks and profitability.

Government Ownership and Strategic National Asset

The GoP maintains a direct shareholding of 22.47% in PSO, with a total of 51% direct and indirect shares. The ratings reflect PSO's important position in the national energy sector, attributed to its oil storage capacity, which represents about half of the country's total storage, and its widespread network across the nation. As a result, the continuous supply of petroleum products to the domestic market and key customers relies on the effective operation of PSO. VIS expects PSO to continue with the retention of its strategic importance for the country and the GoP over the rating horizon.

Environment, Social, and Governance (ESG) framework

PSO has demonstrated a strong commitment to ESG principles, aligning its operations with global sustainability standards. In the environmental domain, the company has prioritized reducing its carbon footprint by initiating a comprehensive carbon emissions study and adopting cleaner technologies. Significant steps include the installation of solar power at the Shikarpur Terminal and afforestation efforts with over 18,000 trees planted at key locations. PSO's ambitious target to achieve net-zero emissions by 2050 and its interim goal of reducing operational carbon emissions by 50% by 2035 underline its strategic focus on environmental stewardship. These initiatives are bolstered by investments in renewable energy and electric vehicle infrastructure, reflecting a forward-looking approach to environmental risks.

On the social front, PSO's emphasis on employee health and safety, community development, and education highlights its commitment to social responsibility. Its robust Health, Safety, and Environment (HSE) framework has delivered commendable results, including ISO 45001 certification and zero fatalities during the year. The introduction of advanced safety technologies, such as a web-based HSE audit platform and e-seal systems for logistics, further enhances operational safety and efficiency. These measures not only mitigate potential ESG-related risks but also strengthen PSO's reputation and operational resilience, critical factors influencing its creditworthiness.

Financial Risk Profile

Profitability Profile

Oil market in Pakistan faces intense competition with more than 38 players competing for market dominance. In the intensely competitive white oil market, the Company expanded its market share to 51.6% (FY23: 51.0%) during FY24. However, by end-September'24, the white oil market share dropped to 45.1%, in the wake of competitive pricing by some private sector players through discounts, not expected to last long.

Net sales increased by ~5% and amounted to Rs. 3.6tr (FY23: Rs. 3.4tr) during FY24. Revenue composition was dominated by petroleum products (69%), followed by LNG (29%), with the remainder attributed to other products. The Company sells its products to dealers, government agencies and autonomous bodies, independent power projects, and other corporate customers. Sales to five major customers of the Company accounted for ~39% (FY23: 40%) during FY24.

Profitability improved during the year with gross and net margins reported at 2.72% (FY23: 2.21%) and 0.44% (FY23: 0.17%) respectively; albeit still weighed down by a negative net margin of -2.69% (FY23: -1.68%) in the LNG segment. The overall improvement is due to an increased selling price of petroleum products, increase in other income from financial assets amounting to Rs. 23.6b (FY23: Rs. 13.5b) and a decreased effective tax rate during FY24. PSO leverages its financial resources to facilitate LNG imports and is currently working on recovering the full transaction costs, including financial charges, from gas companies for which PSO is actively engaged with concerned authorities. Furthermore, profitability is also supported heavily by the lubricants segment, providing support through 22% in net margins to PSO's bottom-line.

Coverage and Liquidity Profiles

Funds from operations (FFO) have slightly recovered during FY24 after the sudden decline in the previous year. FFO stood at Rs. 14.3b (FY23: 9.1b; FY22: Rs. 110.4b). This resulted in an improvement in cashflow coverage. This improvement comes on account of the decrease in income tax paid (FY24: Rs. 25.3b: FY23: Rs. 33.2b). Nevertheless, the Company continues to face challenges posed by circular debt. Interest bearing debt at the end of FY24 was reported at Rs. 411.8b (FY23: Rs. 429.8b). However, liquidity metrics, current ratio and short-term debt coverage stood comfortable at 1.25x (FY23: 1.23x) 1.93x (FY23: 1.87x), respectively.

Capitalization Profile

Equity grew by ~6.8% to Rs. 231.3b (FY23: Rs. 216.5b) during FY24 on the back of increased profit retention. On a timeline basis equity growth has been based on internal generation. Capitalization indicators have shown improvement during FY24 on the back of the overall decrease in debt mix. Gearing and leverage stood at 1.78x (FY23: 1.98x) and 3.21x (FY23: 3.54x), respectively at end-FY24. Debt service coverage ratio also improved during the period to 1.35x (FY23: 0.91x). During the rating horizon, the Company is not planning to do any major CAPEX other than the routine CAPEX for retail and operational investments, which is planned to be funded by internal cash generation. The diversification plans intended are through its subsidiaries, managed by their respective funds. Improvement in capitalization metrics on a continual basis will remain key to the ratings.

Pakistan State Oil Company Limited — Appendix I

Financial Summary

Balance Sheet (PKR Millions)	FY22A	FY23A	FY24A
Property, plant and equipment	15,689.13	18,640.56	22,113.90
Right-of-use Assets	0.00	6,898.28	7,698.64
Stock-in-trade	341,757.89	292,626.15	288,983.14
Trade debts	430,941.59	495,898.44	488,202.27
Cash & Bank Balances	13,919.21	28,954.36	10,725.37
Other Assets	84,338.41	128,877.33	141,239.30
Total Assets	899,454.32	983,396.12	974,448.23
Creditors	0.00	152,889.37	192,985.19
Long-term Debt (incl. current portion)	6,636.98	7,094.64	8,219.19
Short-Term Borrowings	155,845.54	422,705.57	403,553.50
Total Debt	162,482.52	429,800.21	411,772.69
Other Liabilities	521,322.70	184,146.61	138,381.43
Total Liabilities	683,805.22	766,836.19	743,139.31
Paid up Capital	4,694.73	4,694.73	4,694.73
Revenue Reserve	207,231.90	211,861.80	226,610.81
Equity (excl. Revaluation Surplus)	213,408.55	216,559.90	231,308.91

Income Statement (PKR Millions)	FY22A	FY23A	FY24A
Net Sales	2,451,580.83	3,391,111.97	3,571,750.30
Gross Profit	160,995.22	74,846.75	97,290.49
Operating Profit	152,575.77	64,700.73	93,754.62
Finance Costs	4,720.71	40,334.64	52,337.94
Profit Before Tax	147,855.06	24,366.09	41,416.68
Profit After Tax	86,222.52	5,662.14	15,862.54

Ratio Analysis	FY22A	FY23A	FY24A
Gross Margin (%)	6.57%	2.21%	2.72%
Operating Margin (%)	6.22%	1.91%	2.62%
Net Margin (%)	3.52%	0.17%	0.44%
Funds from Operation (FFO) (PKR Millions)	110,363	9,143	14,301
FFO to Total Debt* (%)	67.92%	2.13%	3.47%
FFO to Long Term Debt* (%)	1662.86%	128.87%	173.99%
Gearing (x)	0.76	1.98	1.78
Leverage (x)	3.20	3.54	3.21
Debt Servicing Coverage Ratio* (x)	20.58	0.91	1.35
Current Ratio (x)	1.27	1.23	1.25
(Stock in trade + trade debts) / STD (x)	4.96	1.87	1.93
Return on Average Assets* (%)	13.49%	0.60%	1.62%
Return on Average Equity* (%)	49.57%	2.63%	7.08%
Cash Conversion Cycle (days)	82.00	76.38	62.67

**Annualized, if required*

A - Actual Accounts

P - Projected Accounts

M - Management Accounts

REGULATORY DISCLOSURES						Appendix II
Name of Rated Entity	Pakistan State Oil Company Limited					
Sector	Oil & Gas					
Type of Relationship	Solicited					
Purpose of Rating	Entity Rating					
Rating History	**Rating Date**	**Medium to Long Term**	**Short Term**	**Rating Outlook/ Watch**	**Rating Action**	
	RATING TYPE: ENTITY					
	12/Dec/24	**AA+**	**A1+**	**Stable**	**Reaffirmed**	
	19/Jan/24	AA+	A1+	Stable	Reaffirmed	
	13/Dec/22	AA+	A1+	Stable	Reaffirmed	
	03/Dec/21	AA+	A1+	Stable	Reaffirmed	
	08/Dec/20	AA+	A1+	Stable	Maintained	
	04/May/20	AA+	A1+	RW - Dev	Maintained	
	19/Jun/19	AA+	A1+	Stable	Initial	
Instrument Structure	N/A					
Statement by the Rating Team	VIS, the analysts involved in the rating process and members of its rating committee do not have any conflict of interest relating to the credit rating(s) mentioned herein. This rating is an opinion on credit quality only and is not a recommendation to buy or sell any securities.					
Probability of Default	VIS ratings opinions express ordinal ranking of risk, from strongest to weakest, within a universe of credit risk. Ratings are not intended as guarantees of credit quality or as exact measures of the probability that a particular issuer or particular debt issue will default.					
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Due Diligence Meetings Conducted	**Name**	**Designation**	**Date**			
	Mr. Ismail Abdul Rauf	Manager Reporting	28 Nov 2024			
	Ms. Gulbakht Mangi	Financial Reporting Associate	28 Nov 2024			