# RATING REPORT

# Oil & Gas Development Company Limited

**REPORT DATE:**
January 24, 2020

**RATING ANALYSTS:**
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## RATING DETAILS

| Rating Category | Latest Rating | | Previous Rating | |
|---|---|---|---|---|
| | **Long-term** | **Short-term** | **Long-term** | **Short-term** |
| **Entity** | AAA | A-1+ | AAA | A-1+ |
| **Rating Outlook** | *Stable* | | *Stable* | |
| **Rating Date** | *January 20, '20* | | *February 15, '19* | |

## COMPANY INFORMATION

| | |
|---|---|
| Incorporated in 1997 | **External auditors:** KPMG Taseer Hadi & Co., Chartered Accountants and A.F. Ferguson & Co., Chartered Accountants |
| Public Limited Company | **Chairman of the Board:** Dr. Qamar Javaid Sharif<br>**Acting MD/CEO:** Dr. Naseem Ahmad |
| **Key Shareholders (with stake 5% or more):** | |
| Government of Pakistan – 67.48%<br>OGDCL – Employees Empowerment Trust – 10.05%<br>Ministry of Privatization and Investment – 7.50% | |

## APPLICABLE METHODOLOGY(IES)

**VIS Entity Rating Criteria: Corporates (May 2019)**
*https://www.vis.com.pk/kc-meth.aspx*

# Oil & Gas Development Company Limited

## OVERVIEW OF THE INSTITUTION

Oil & Gas Development Company Limited (OGDCL) was incorporated as a Public Limited Company in October 1997. Core business activities of the Company involve exploration, development and production of oil and gas resources, including their sale and related activities.

**Profile of Chairman:**
Dr. Sharif is a Petroleum Engineer with over 35 years of experience in the oil and gas industry, across multiple disciplines. He completed his MS and PhD in Petroleum Engineering from Texas A&M University, College Station, Texas, USA and his B.Sc. Mining Engineering from University of Engineering and Technology (UET) Lahore, Pakistan.

**Profile of MD/CEO:**
Dr. Naseem Ahmad assumed the charge of MD/CEO on acting basis w.e.f. August 1, 2019. He holds a Ph.D. in Petroleum Engineering from Imperial College, London, and M.Sc. in Petroleum Engineering from the University of Texas at Austin, U.S.A. and B.Sc. in Petroleum Engineering from UET Lahore, Pakistan.

**Financial Snapshot:**
**Total Equity:**
1QFY20: Rs. 652.7b;
FY19: Rs. 625.4b;
FY18: Rs. 550.6b
**Total Assets:**
1QFY20: Rs. 783.1b;
FY19: Rs. 766.6b;
FY18: Rs. 666.5b
**Profit After Tax**:
1QFY20: Rs. 27.3b;
FY19: Rs. 118.4b;

## RATING RATIONALE

The assigned ratings of Oil & Gas Development Company Limited (OGDCL) incorporate its ownership structure with majority shares held by the Government of Pakistan. The low business risk of the company emanates from its robust margins, providing considerable cushion against volatility in international oil prices. Moreover, OGDCL is the leading Company in exploration and production sector of Pakistan. The Company has an assured product off-take amid excess demand of oil & gas vis-à-vis local supply. During FY19, OGDCL registered healthy growth in revenue and profits, driven largely by higher LPG production, considerable increase in the average realized price of hydrocarbons and rupee depreciation. The ratings also take into account low financial risk profile, emanating from debt-free capital structure and strong liquidity indicators. Despite rising trend in industry-wide inter-corporate debt, the Company continues to manage its capital expenditure requirements through internal cash flows.

**Key Rating Drivers**

**Continuation of exploration led growth strategy**

OGDCL is the largest E&P Company in Pakistan with 38% share of total area under exploration, having 20 owned and 25 operated joint venture exploration licenses at end-1QFY20. The Company also holds working interest in 6 exploration blocks operated by other E&P companies. OGDCL spud 16 wells during FY19 (FY18: 20 wells), out of which 9 were exploratory/appraisal wells and 7 were development wells. Number of wells spud stood at 2 during 1QFY20, including 1 exploratory and 1 development well. Moreover, drilling and testing of 7 wells pertaining to the previous fiscal years were also completed during the quarter. Exploratory efforts led to 3 new oil and gas discoveries during FY19 (FY18: 4), having cumulative daily production potential of 915 barrels of oil and 12.89 MMcf of gas. Another 3 discoveries were made during 1QFY20 at Pandhi-1, Togh-1 and Chanda-5, having cumulative daily production potential of 826 barrels of oil and 22 MMcf of gas.

OGDCL continued to focus on completion of its ongoing development projects in order to optimize oil, gas and LPG production. In this regard, the EPCC contract for Nashpa compression project has been awarded and preliminary design work is underway. Expected completion date of the project is June 2020. Meanwhile, the Company completed the installation work with respect to gas processing facilities at Dhok Hussain in FY19 while upgradation of plant facilities at Mela field and laying of gas pipeline to Nashpa plant for LPG extraction was completed in December 2019. Qadirpur and Uch compression projects are also in progress and are expected to be completed by December 2020 and December 2021, respectively.

**OGDCL maintained market leadership position**

OGDCL maintained its leading position in E&P sector during 1QFY20. Its share in crude oil and gas stood at 47% (FY19: 45%; FY18: 47%) and 29% (FY19: 29%; FY18: 29%) respectively. The average daily net saleable crude oil production decreased to 37,650 barrels (FY19: 40,810 barrels; FY18: 41,278 barrels) and gas production decreased to 960 MMcf (FY19: 1,104 MMcf; FY18: 1,022 MMcf). The average daily production of LPG clocked at 702 tons (FY19: 802 tons; FY18: 690 tons). The overall production levels were affected by natural decline at Rajian, Tando Alam, Sinjhoro, and Qadirpur fields and annual turnaround of plant at Nashpa, KPD-TAY, Chanda and Bobi fields. Moreover, turbine issues at UPL-I & II also contributed towards lower production of hydrocarbons during the period. During 1QFY20, OGDCL not only completed installation of electrical submersible pump at Pasahki-5 – which produced a positive impact of 21,500 barrels – but also injected development well 'Qadirpur-61' in the production system which yielded gross production of 154 MMcf. The reserve life for oil and gas fields on 2P (Proven and Probable) basis was 14 years at end-1QFY20 (1QFY19: 12 years; 1QFY18: 12 years).

**Growth in sales and profitability emanating from favorable pricing and rupee depreciation**

OGDCL reported higher net revenue of Rs. 261.5b during FY19 (FY18: Rs. 205.3b), driven largely by considerable increase in the average realized price of crude oil, gas and LPG. Gas remained the leading contributor in gross revenue with Rs. 156.9b (FY18: Rs. 127.6b), followed by crude oil with Rs. 116.8b (FY18: Rs. 90.7b), LPG with Rs. 24.2b (FY18: 17.3b) and others with Rs. 527m (FY18: Rs. 434m). Growth in revenue mainly emanated from higher average realized crude oil price of Rs. 8,021 per bbl during FY19 (FY18: Rs. 6,007 per bbl), gas price of Rs. 336.62 per mcf (FY18: Rs. 258.93 per mcf) and LPG price of Rs. 65,512 per ton (FY18: Rs. 55,666 per ton). Moreover, the increase in average exchange rate to Rs. 136.55/US$ (FY18: Rs. 110.09/US$) also underpinned revenue growth during the fiscal year. Resultantly, OGDCL reported higher gross profit of Rs. 167.1b (FY18: Rs. 121.5b) with improved margin of 63.9% (FY18: 59.2%). Given lower cost of dry and abandoned wells, the Company's exploration and prospecting expenditure decreased to Rs. 12.5b (FY18: Rs. 16.2b). The Company

FY18: Rs. 78.7b

recorded increase in other income to Rs. 32.3b during FY19 (FY18: Rs. 16b) owing to higher exchange gain of Rs. 13b (FY18: Rs. 3b) and return on investments and bank deposits of Rs. 15.9b (FY18: Rs. 11b). Accounting for tax expense, net income stood higher at Rs. 118.4b (FY18: Rs. 78.7b) with notably improved margin of 45.3% (FY18: 38.3%).

Net revenue amounted to Rs. 66.2b during 1QFY20 as the impact of decline in production levels was offset by higher average exchange rate of Rs. 158.28/US$ and favorable pricing. The average realized price of crude oil was recorded higher at Rs. 8,340 per bbl and gas price at Rs. 386.6 per mcf, partially offset by lower LPG price of Rs. 57,032 per ton during the period. Thereby, gross profit amounted to Rs. 43.2b with further improvement in margin to 65.2%. Accounting for tax expense, net profit stood at Rs. 27.3b during 1QFY20, though net margin decreased to 41.3% mainly on account of increase in exploration and prospecting expenditure due to two dry wells.

**Higher asset base mainly manifested in trade debts (due to accumulation on account of inter-corporate debt) and higher investment portfolio**

Asset base augmented to Rs. 783.1b by end-1QFY20 (FY19: Rs. 766.6b; FY17: Rs. 666.5b) mainly on account of higher investment portfolio and trade debts. Total investment portfolio, inclusive of current portion, increased to Rs. 141.3b (FY19: Rs. 136.7b; FY18: Rs. 123.6b), including investment in Mari Petroleum Company Limited of Rs. 14.2b (FY19: Rs. 12.7b), T-bills of Rs. 11.5b (FY19: Rs. 10.2b) and TFCs of Rs. 115.6b (FY19: Rs. 113.7b). The investment portfolio is inclusive of PPTFCs amounting Rs. 82.0b issued by Power Holding (Pvt.) Limited (PHPL) for partial resolution of inter-corporate debt. Although the said instrument continues to remain non-performing, comfort is drawn on the back of sovereign guarantee provided by GoP on the related principal and mark-up. Trade debts increased to Rs. 264.2b by end-1QFY20 (FY19: Rs. 242.7b; FY18: Rs. 163.7b) mainly due to higher inter-corporate debt of Rs. 217.7b (FY19: Rs. 194.2b; FY18: Rs. 121.3b). Other financial assets remained largely stable at Rs. 74.9b (FY19: Rs. 74.7b), representing TDRs of Rs. 47.6b (FY19: Rs. 48.3b), T-bills of Rs. 27.1b (FY19: Rs. 26.2b) and National Investment Trust (NIT) fund units of Rs. 221.5m (FY19: Rs. 247m). OGDCL held Rs. 8.5b in cash and bank balance at end-1QFY20 (FY19: Rs. 20.6b; FY18: Rs. 3.7b).

**Liquidity position underpinned by healthy cash flows generation and debt-free balance sheet**

Liquidity position of the Company is underpinned by healthy cash flows generation and sizeable investment portfolio. OGDCL generated Rs. 22.5b in funds from operations (FFO) during 1QFY20 (FY19: Rs. 139.7b; FY18: Rs. 97.1b). Current ratio improved further to 8.51x by end-1QFY20 (FY19: 7.02x; FY18: 7.35x) on account of lower trade and other payables of Rs. 39b (FY19: Rs. 49.5b) and higher trade debts. OGDCL continued to maintain debt-free balance sheet, whereas equity base augmented to Rs. 652.7b by end-1QFY20 (FY19: Rs. 625.4b; FY18: Rs. 550.6b) with the retention of profits.

**Satisfactory compliance with Code of Corporate Governance**

All the nominations on the Board of Directors (BoD) are made by the GoP. The BoD comprises government officials and experienced professionals having considerable experience in the oil and gas sector. OGDCL meets the minimum regulatory requirement related to number of independent directors in the BoD. In order to ensure effective implementation of sound internal control system and compliance with the Code of Corporate Governance, OGDCL has formed 6 Board committees, namely i) Audit Committee, ii) HR & Nomination Committee, iii) Risk Management & Security Committee, iv) Procurement, Operations & Finance Committee v) Transformation Committee and vi) CSR Committee. Dr. Naseem Ahmad is currently serving as the acting MD/CEO. OGDCL also has an independent internal audit department, the scope and role of which is approved by the BoD, whilst the head of internal audit reports directly to the Audit Committee. The Board has established a system of sound internal control and set in place adequate systems and controls to ensure that an appropriate control environment exists in the Company spanning E&P activities, financial reporting and compliance activities.

## Oil & Gas Development Company Limited Annexure I

| FINANCIAL SUMMARY (*amounts in PKR billions*) | | | |
|---|---|---|---|
| **BALANCE SHEET** | **FY18** | **FY19** | **1QFY20** |
| **Property, Plant and Equipment** | 124.1 | 117.8 | 116.8 |
| **Development and Production Assets – Intangible** | 94.4 | 92.0 | 93.2 |
| **Long-term Investments (incl. current maturity)** | 123.6 | 136.7 | 141.3 |
| **Other Non-Current Assets** | 14.5 | 24.2 | 24.8 |
| **Other Financial Assets** | 67.8 | 74.7 | 74.9 |
| **Trade Debts** | 163.7 | 242.7 | 264.2 |
| **Income Tax – Advance** | 37.3 | 20.0 | 19.3 |
| **Cash & Bank Balances** | 3.7 | 20.6 | 8.5 |
| **Other Current Assets** | 37.4 | 38.0 | 40.1 |
| **Total Assets** | **666.5** | **766.6** | **783.1** |
| **Trade and Other Payables** | 36.7 | 49.5 | 39.0 |
| **Non-current Liabilities** | 60.7 | 68.6 | 68.9 |
| **Short Term Borrowings** | - | - | - |
| **Long Term Financing** ***(Inc. current maturity)*** | - | - | - |
| **Other Current Liabilities** | 18.5 | 23.2 | 22.5 |
| **Total Liabilities** | **115.9** | **141.2** | **130.4** |
| **Total Equity** | **550.6** | **625.4** | **652.7** |
| **Paid-Up Capital** | 43.0 | 43.0 | 43.0 |
| | | | |
| **INCOME STATEMENT** | **FY18** | **FY19** | **1QFY20** |
| **Net Sales** | 205.3 | 261.5 | 66.2 |
| **Gross Profit** | 121.5 | 167.1 | 43.2 |
| **Profit Before Tax** | 112.6 | 176.6 | 39.7 |
| **Profit After Tax** | 78.7 | 118.4 | 27.3 |
| **FFO** | 97.1 | 139.7 | 22.5 |
| | | | |
| **RATIO ANALYSIS** | **FY18** | **FY19** | **1QFY20** |
| **Gross Margin (%)** | 59.2 | 63.9 | 65.2 |
| **Net Margin (%)** | 38.3 | 45.3 | 41.3 |
| **FFO to Long-Term Debt** | - | - | - |
| **FFO to Total Debt** | - | - | - |
| **Debt Servicing Coverage Ratio (x)** | - | - | - |
| **ROAA (%)** | 12.2 | 16.5 | 14.1* |
| **ROAE (%)** | 14.8 | 20.1 | 17.1* |
| **Current Ratio** | 7.35 | 7.02 | 8.51 |
| **Dividend Payout Ratio (%)** | 54.6 | 40.0 | 39.4 |

* *Annualized*

## ISSUE/ISSUER RATING SCALE & DEFINITIONS — Annexure II

**VIS** Credit Rating Company Limited

### RATING SCALE & DEFINITIONS: ISSUES / ISSUERS

**Medium to Long-Term**

**AAA**
Highest credit quality; the risk factors are negligible, being only slightly more than for risk-free Government of Pakistan's debt.

**AA+, AA, AA-**
High credit quality; Protection factors are strong. Risk is modest but may vary slightly from time to time because of economic conditions.

**A+, A, A-**
Good credit quality; Protection factors are adequate. Risk factors may vary with possible changes in the economy.

**BBB+, BBB, BBB-**
Adequate credit quality; Protection factors are reasonable and sufficient. Risk factors are considered variable if changes occur in the economy.

**BB+, BB, BB-**
Obligations deemed likely to be met. Protection factors are capable of weakening if changes occur in the economy. Overall quality may move up or down frequently within this category.

**B+, B, B-**
Obligations deemed less likely to be met. Protection factors are capable of fluctuating widely if changes occur in the economy. Overall quality may move up or down frequently within this category or into higher or lower rating grade.

**CCC**
Considerable uncertainty exists towards meeting the obligations. Protection factors are scarce and risk may be substantial.

**CC**
A high default risk

**C**
A very high default risk

**D**
Defaulted obligations

**Short-Term**

**A-1+**
Highest certainty of timely payment; Short-term liquidity, including internal operating factors and /or access to alternative sources of funds, is outstanding and safety is just below risk free Government of Pakistan's short-term obligations.

**A-1**
High certainty of timely payment; Liquidity factors are excellent and supported by good fundamental protection factors. Risk factors are minor.

**A-2**
Good certainty of timely payment. Liquidity factors and company fundamentals are sound. Access to capital markets is good. Risk factors are small.

**A-3**
Satisfactory liquidity and other protection factors qualify entities / issues as to investment grade. Risk factors are larger and subject to more variation. Nevertheless, timely payment is expected.

**B**
Speculative investment characteristics; Liquidity may not be sufficient to ensure timely payment of obligations.

**C**
Capacity for timely payment of obligations is doubtful.

**Rating Watch:** VIS places entities and issues on 'Rating Watch' when it deems that there are conditions present that necessitate re-evaluation of the assigned rating(s). Refer to our 'Criteria for Rating Watch' for details. www.vis.com.pk/images/criteria_watch.pdf

**Rating Outlooks:** The three outlooks 'Positive', 'Stable' and 'Negative' qualify the potential direction of the assigned rating(s). An outlook is not necessarily a precursor of a rating change. Refer to our 'Criteria for Rating Outlook' for details.www.vis.com.pk/images/criteria_outlook.pdf

**(SO) Rating:** A suffix (SO) is added to the ratings of 'structured' securities where the servicing of debt and related obligations is backed by some sort of financial assets and/or credit support from a third party to the transaction. The suffix (SO), abbreviated for 'structured obligation', denotes that the rating has been achieved on grounds of the structure backing the transaction that enhanced the credit quality of the securities and not on the basis of the credit quality of the issuing entity alone.

**(blr) Rating:** A suffix (blr) is added to the ratings of a particular banking facility obtained by the borrower from a financial institution. The suffix (blr), abbreviated for 'bank loan rating' denotes that the rating is based on the credit quality of the entity and security structure of the facility.

**'p' Rating:** A 'p' rating is assigned to entities, where the management has not requested a rating, however, agrees to provide informational support. A 'p' rating is shown with a 'p' subscript and is publicly disclosed. It is not modified by a plus (+) or a minus (-) sign which indicates relative standing within a rating category. Outlook is not assigned to these ratings. Refer to our 'Policy for Private Ratings' for details. www.vis.com.pk/images/policy_ratings.pdf

**'SD' Rating:** An 'SD' rating is assigned when VIS believes that the ratee has selectively defaulted on a specific issue or obligation but it will continue to meet its payment obligations on other issues or obligations in a timely manner.

## REGULATORY DISCLOSURES — Appendix III

| | |
|---|---|
| **Name of Rated Entity** | Oil & Gas Development Company Limited |
| **Sector** | Oil & Gas |
| **Type of Relationship** | Solicited |
| **Purpose of Rating** | Entity Ratings |

**Rating History**

| Rating Date | Medium to Long Term | Short Term | Rating Outlook | Rating Action |
|---|---|---|---|---|
| **RATING TYPE: ENTITY** | | | | |
| 20/01/2020 | AAA | A-1+ | Stable | Reaffirmed |
| 15/02/2019 | AAA | A-1+ | Stable | Reaffirmed |
| 22/02/2018 | AAA | A-1+ | Stable | Reaffirmed |

| | |
|---|---|
| **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. Fahad Saeed | Accountant | December 31, '19 |