Day Break

Tuesday, 24 October 2017

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COMPANY UPDATE

PAKISTAN STATE OIL COMPANY LIMITED
OIL & GAS MARKETING COMPANIES

Recommendation		BUY
Target Price:		441.5
Last Closing:	23-Oct-17	358.3
Upside:		23.2
Valuation Methodology:		Discounted Cash Flow (DCF)
Time Horizon:		Jun-18

Market Data

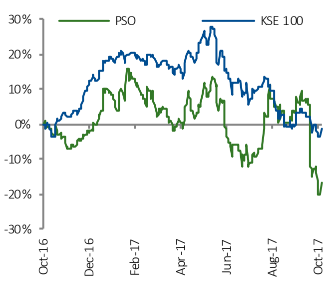
Bloomberg Tkr.		PSO PA
Shares (mn)		326.0
Free Float Shares (mn)		146.7
Free Float Shares (%)		45.0%
Market Cap (PKRbn | USDmn)	116.8	1,108.6
Exchange		KSE 100

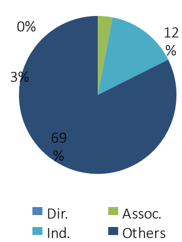
Price Info.	90D	180D	365D
Abs. Return	(9.3)	(20.4)	(17.3)
Lo	335.1	335.1	335.1
Hi	466.6	475.3	486.1

Key Company Financials
Period End: Jun

PKRbn	FY16A	FY17A	FY18E	FY19F
Total Revenue	678.0	878.1	885.5	982.8
Net Income	10.3	18.2	18.0	18.0
EPS (PKR)	31.5	55.9	55.4	55.2
DPS (PKR)	12.5	25.0	20.0	20.0
Total Assets	342.3	392.4	318.8	339.7
Total Equity	91.6	102.8	114.9	126.4
Key Financial Ratios				
ROE (%)	11.2	17.7	15.7	14.2
P/E (x)	11.4	6.4	6.5	6.5
P/B (x)	1.3	1.1	1.0	0.9
DY (%)	3.5	7.0	5.6	5.6

Relative Price Performance & Shareholding





About the Company

Pakistan State Oil was incorporated in Pakistan in 1976. 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.

Source: Bloomberg, PSX & IGI Research

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Oil & Gas – Marketing Companies

PSO: Analyst Briefing Takeaway 1QFY18

- Pakistan State Oil Company Limited (PSO) held its analyst briefing on 23rd Oct-17 to discuss financial result for 1QFY18 and future prospects of the company. The company reported earnings of PKR 5.03bn (EPS PKR 18.51) up by +15%YoY during 1QFY18 as compared to PKR 4.38bn (EPS PKR 16.11) in the same period last year;
- Earnings were primarily driven by a) 30.1%/31.4% YoY rise in MS/HSD sales, b) 7.6%/35.9%/49.9%YoY increase in Jet fuel/Lubes/LNG sales, c) increase in FO margin per Mton by +21%YoY to PKR 1,090/Mton, d) +16%YoY incline in other income and e) 41%YoY drop in finance cost.
- We maintain a **'BUY'** call on PSO with Jun-18 TP of PKR 442/share (ex-bonus) offering an upside of +23% from its last close. The company is currently trading at FY18E P/E of 6.5x and dividend yield of 5.6%.

Earnings for 1QFY18 reported at PKR 18.51/share up by +15%YoY

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Lower tax lifts earnings on a quarterly basis by +24%QoQ in 1QFY18

PSO reported earnings of PKR 4.07bn (EPS PKR 14.98) during 1QFY18 up by +24%QoQ primarily owing to a) lower effective tax rate of 32% compared to 47% in 4QFY17, b) 53%QoQ decline in finance cost and, c) +25%/+5%/+2%QoQ rise in MS/HSD/FO sales. To recall, PSO incurred super tax charge in 4QFY17 which resulted in higher effective tax rate.

Exhibit:

PSO Financial Highlights

PKRmn	1QFY18	1QFY17	YoY	4QFY17	QoQ
Net Sales	258,645	193,512	34%	248,638	4%
Gross Profit	9,190	9,705	-5%	10,075	-9%
Operating Costs	3,385	3,680	-8%	3,612	-6%
Other Op. Income	2,213	1,909	16%	2,726	-19%
EBIT	8,326	7,935	5%	9,189	-9%
Finance Cost	756	1,279	-41%	1,592	-53%
Profit Before Taxation	7,420	6,786	9%	7,670	-3%
Taxation	2,390	2,410	-1%	3,601	-34%
Profit After Taxation	5,029	4,376	15%	4,069	24%
EPS (PKR)	18.51	16.11		14.98	
EPS Diluted (PKR)	15.43	13.42		12.48	
DPS (PKR)	-	-		15.00	

Source: IGI Research, Company Financials, PSX — *Shares mn: 326.02 mn*

Receivables Position for PSO

PKR'bn	Oct-17	Sep-17	Jun-17
Power Sector	197.5	188.3	176.2
LNG	5.7	4.0	14.0
PIA	13.3	13.1	13.3
PDC	9.6	9.6	9.6
Total	**226.1**	**215.0**	**213.1**
LPS	76.4	76.4	73.7
Total Inclusing LPS	**302.5**	**291.4**	**286.8**

MS, HSD and FO Margins

PKR	Oct-17	1QFY18	1QFY17
MS (per ltr)	2.41	2.45	2.39
HSD (per ltr)	2.41	2.34	2.39
FO (per Mton)	1,392	1,090	899

Exhibit: Market Share - Company wise (1QFY18)

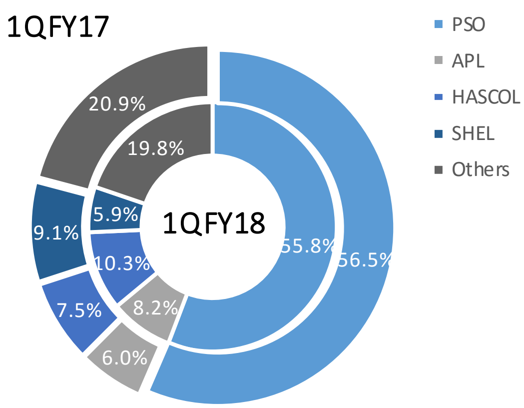
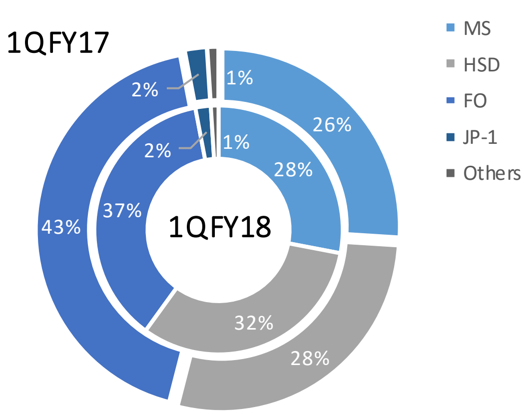


Exhibit: POL Consumption - Product wise (1QFY18)



Source: Company Financials, IGI Research

Major highlights of analyst briefing as stated by the management

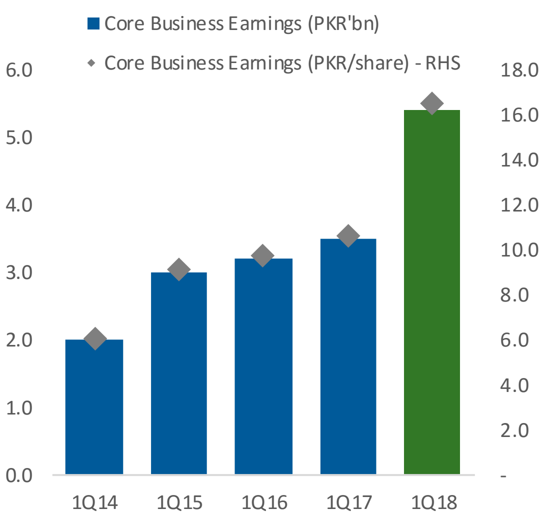
Key takeaway of the analyst briefing included:

- PSO plans to increase its storage capacity by nearly 250k Mton;
- Receivables from power sector have crept up to PKR 198bn as at Oct-17 from PKR 176bn as at Jun-17, however recoveries were made on LNG front from SNGP;
- The company is focusing on cash sales on FO to avoid cash constraints and through continuous efforts better recoveries have been witnessed from HUBCO;
- PSO's outstanding LPS stands at PKR 76.4bn;
- The company is currently utilizing FE-25 which stands at USD 750mn which offers a lower financing cost thus leading to lower finance cost;
- HSD deregulation has been notified but the company has not received any letter from the Government and is still in the process of panning out a plan for implementation;
- PSO being the market leader will not misuse the deregulation of HSD margins and will keep the margin increase within CPI inflation;
- Government has assured PSO that it will reimburse the differential amount of loss in case of PKR devaluation. The company booked And kept PKR 2.4bn gain as liability when exchange rate came down and will first utilize that gain in case of PKR devaluation and then go to Government;
- Company is currently selling HOBC at OMC margin of PKR 6.3/ltr;

Key Result highlights included:

- In the absence of PIB income, other income was compensated by a Late Payment Surcharge (LPS) income of PKR 1.3bn compared to a total of PKR 1.2bn of PIB and LPS income reported in the same period last year;
- Finance cost declined substantially as proceeds from PIB maturity were utilized to pay off short-term borrowings and lower cost of borrowing on FE-25 loan;
- The company incurred an inventory loss of PKR 0.7bn in 1QFY18 compared to PKR 1.0bn in the same period last year;
- FO profit margin up to PKR 1,090/Mton during 1QFY18 compared to PKR 899/Mton in the corresponding period last year and currently standing at PKR 1,392/Mton;
- PSO captured SHELs market share to post 30.1%/31.4%/7.6%/35.9%YoY growth in MS/HSD/Jet fuel/Lubes sales, LNG sales were up by 49.9%YoY.

Highest ever core earnings in 1Q before inventory gain/losses, interest income & expenses



Source: Company Financials, IGI Research

Outlook

The company further expects to increase its retail outlets to cater rising demand and company under performance compared to industry growth. Furthermore, FO profit contribution (up by +21%YoY in 1QFY18) is expected to lift profitability as margins are deregulated and linked with landed cost price. The Company is expected to increase it storage capacity by 250k MTon in the coming years which is expected to reduce PSO's vulnerability to heavy inventory loss/gain and ease storage concerns especially for MS. Furthermore, increased marketing and sales promotion for lubes should provide a healthy growth in the segment. Continuation of LNG business, increased volumes and LPS income to partially offset decline in other income.

Recommendation

We have tweaked our earnings estimates by +1%-2% based on lower finance cost. however based on rising receivables we have revised down our target price by 1% to PKR 442/share from previous PKR 445/share. We maintain a **'BUY'** call on PSO with Jun-18 TP of PKR 442/share (ex-bonus) offering an upside of +23% from its last close. The company is currently trading at FY18E P/E of 6.5x and dividend yield of 5.6%.

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Recommendation	Rating System
Buy	If target price on aforementioned security(ies) is more than 10%, from its last closing price(s)
Hold	If target price on aforementioned security(ies) is in between -10% and 10%, from its last closing price(s)
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Time Horizon: Jun – 2018

Valuation Methodology: The analyst(s) has used following valuation methodology to arrive at the target price of the said security (ies):
DCF (Discounted Cash Flow)

Risk: Investment in securities are subject to economic risk, market risk, interest rate risks, currency risks, credit risks, political and geopolitical risks. The performance of company(ies) covered herein mightunfavorably be affected by multiple factors including, business, economic, and political conditions. Hence, there is no assurance or guarantee that estimates, recommendation, opinion, etc. given about the security(ies)/company(ies) in the report will be achieved.

Basic Definitions and Terminologies used: Target Price: A price target is the projected price level of a financial security stated by an investment analyst or advisor. It represents a security's price that, if achieved, results in a trader recognizing the best possible outcome for his investment. **Market Cap.:** Market capitalization is calculated by multiplying a company's shares outstanding by current trading price. **ROE:** Return on equity is the amount of net income returned as a percentage of shareholders' equity. **P/E:** Price to Earnings ratio of a company's share price to its per-share earnings. **P/B:** Price to Book ratio used to compare a stock's market value to its book value. **DY:** The dividend yield is dividend per share, divided by the price per share.

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