Day Break

Wednesday, 09 August 2017

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COMPANY UPDATE

PAKISTAN STATE OIL COMPANY LIMITED
OIL & GAS MARKETING COMPANIES

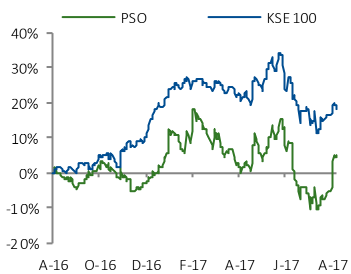
Recommendation		BUY
Target Price:		519.1
Last Closing:	8-Aug-17	454.1
Upside:		14.3
Valuation Methodology:		Discounted Cash Flow (DCF)
Time Horizon:		Dec-17

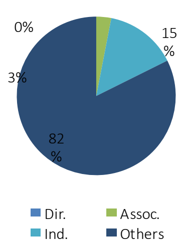
Market Data			
Bloomberg Tkr.			PSO PA
Shares (mn)			271.7
Free Float Shares (mn)			122.3
Free Float Shares (%)			45.0%
Market Cap (PKRbn | USDmn)		123.4	1,170.9
Exchange			KSE 100
Price Info.	90D	180D	365D
Abs. Return	(1.7)	(10.1)	5.0
Lo	368.4	368.4	368.4
Hi	475.3	481.1	486.1

Key Company Financials
Period End: Jun

PKRbn	FY16A	FY17E	FY18F	FY19F
Total Revenue	678.0	878.1	963.5	1,070.9
Net Income	10.27	18.2	19.5	22.6
EPS (PKR)	37.8	67.1	71.8	83.1
DPS (PKR)	12.5	25.0	22.0	25.0
Total Assets	342.3	379.4	412.1	422.1
Total Equity	91.6	105.9	119.4	135.2
Key Financial Ratios				
ROE (%)	11.2	17.2	16.3	16.7
P/E (x)	12.0	6.8	6.3	5.5
P/B (x)	1.3	1.2	1.0	0.9
DY (%)	2.8	5.5	4.8	5.5

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, KSE 100 & IGI Research

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Oil & Gas – Marketing Companies

PSO: Analyst Briefing Takeaway FY17

- Pakistan State Oil Company Limited (PSO) held its analyst briefing on 08th Aug-17 to discuss financial results for FY17 and reported earnings of PKR 18.23bn (EPS PKR 67.08) up by +77%YoY during FY17 as compared to PKR 10.27bn (EPS PKR 37.81). The company announced higher than expected cash dividend of PKR 15.0/share (total FY17 cash dividend of PKR 25/share) along with the result, accompanied by a surprise bonus share of 20%.
- The company reported earnings of PKR 14.16bn (EPS PKR 52.10) during 9MFY17 as compared to PKR 4.59bn (EPS PKR 16.91) in the same period last year.
- We maintain a **'BUY'** call on PSO with Dec-17 TP of PKR 519/share offering an upside of +14% from its last close. The company is currently trading at FY18E P/E of 6.3x and dividend yield of 4.8%.

Earnings for FY17 reported at PKR 67.08/share, accompanied by 20% bonus share

Pakistan State Oil Company Limited (PSO) held its analyst briefing on 08th Aug-17 to discuss financial results for FY17 and future prospects of the company. The company reported earnings of PKR 18.23bn (EPS PKR 67.08) up by +77%YoY during FY17 as compared to PKR 10.27bn (EPS PKR 37.81) in the same period last year. Earnings during FY17 were primarily driven by a) after tax inventory gains of PKR 1.06bn (PKR 3.9/share) as compared to an inventory loss of PKR 5.29bn (PKR 19.5/share) in the same period last year, b) +5%/+10%YoY rise in white/black oil sales led by +9%/+18%/+11%YoY rise in MS/Jet Fuel/FO volumes, c) increase in FO margin by +7%YoY to PKR 1,021/Mton and, d) +28%YoY jump in Lubricant sales. To highlight, PSO reported it's highest ever core earnings before inventory gain/losses, interest income and expenses of PKR 16.2bn (~PKR 59.6/share) in FY17. The company announced higher than expected cash dividend of PKR 15.0/share (total FY17 cash dividend of PKR 25/share) along with the result, accompanied by a surprise bonus share of 20%.

4QFY17 earnings down by 28%YoY to PKR 14.98/share

PSO reported earnings of PKR 4.07bn (EPS PKR 14.98) during 4QFY17 as compared to PKR 5.68bn (EPS PKR 20.90) in the same period last year. This drop in earnings is primarily attributable to a) after tax inventory gains of PKR 591mn, b) 54%YoY decline in other income owing to lower late payment surcharge (LPS) income and, c) effective tax rate stood at 46.9% during 4QFY17 (4QFY16: 40.6%).

Exhibit:

Financial Highlights

PKRmn	4QFY17	4QFY16	YoY	QoQ	FY17	FY16	YoY
Net Sales	248,649	189,380	31%	14%	878,147	677,967	30%
Gross Profit	10,158	9,222	10%	10%	37,199	22,863	63%
Operating Costs	3,694	3,399	9%	27%	13,282	12,835	3%
Other Op. Income	2,726	5,870	-54%	60%	10,745	12,798	-16%
Finance Cost	1,592	2,135	-25%	7%	5,923	7,150	-17%
PBT	7,670	9,558	-20%	14%	29,347	16,289	80%
PAT	4,069	5,680	-28%	-2%	18,226	10,273	77%
EPS (PKR)	**14.98**	**20.90**			**67.08**	**37.81**	
DPS (PKR)	15.00	7.50			20.00	12.50	
Bonus	20%	-			-	-	

Source: IGI Research, Company Financials *Shares mn: 271.69 mn*

Exhibit: Receviables Position for PSO

PKR'bn	Aug-17	FY17	FY16
Pow er Sector	184.2	176.1	146.5
LNG	2.7	14.0	11.0
PIA	13.6	13.3	12.3
PDC	9.6	9.6	9.6
Total	**210.1**	**213.0**	**179.4**

Exhibit: MS, HSD and FO Margins

PKR	Current	FY17	FY16
MS (per ltr)	2.41	2.36	2.31
HSD (per ltr)	2.41	2.30	2.26
FO (per Mton)	1,243	1,021	958

Exhibit: Market Share - Company w ise (FY17)

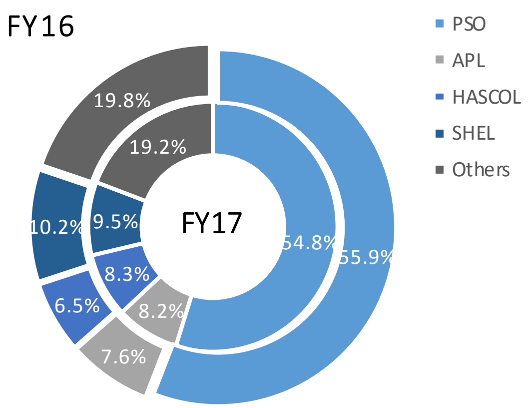
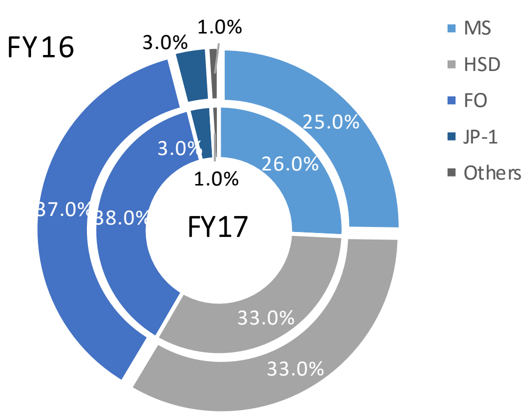


Exhibit: POL Consumption - Product w ise (FY17)



Source: Company Financials, IGI Research

Major highlights of analyst briefing as stated by the management

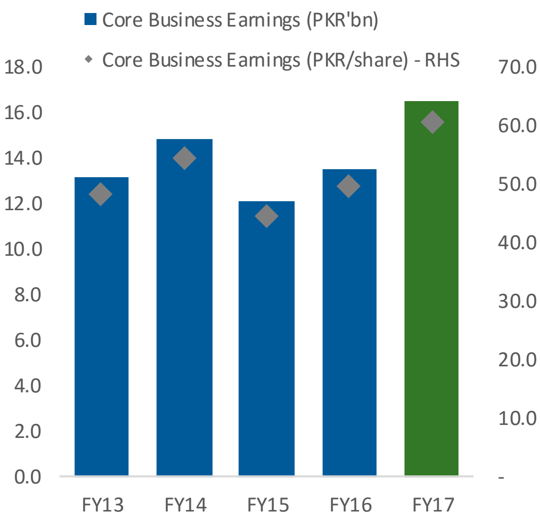
Key takeaway of the analyst briefing included:

- PSO plans to invest ~PKR 40bn over the next 3 years primarily to enhance storage capacity and also to improve and build internal pipelines and automation projects at retail outlets,
- The oil tanker up gradation imposed by OGRA will not impact PSO (other OMC as well) as the company does not own those tankers and operate with them on contractual basis,
- The company is now receiving 6 shipments per month of LNG and as a result LNG volumes grew by +82%YoY rise to 3.5mn Ton in FY17,
- PSO still awaits clarity on shift of LNG business to Pakistan LNG Ltd. For which the previous deadline communicated by the Government was Dec-16 then was extended to Jul-17. However, the company stated the LNG business to remain with PSO as there has been no update from the Government in recent times
- Even after LNG supply arrangement is shifted from PSO to Pakistan LNG, the company plans to remain in LNG marketing business,
- Case against PSO withdrawn in the Supreme Court for increasing its shareholding in PRL; the company expect to incur Capex to double the refining capacity,
- The company plans to open retail outlets close to Gwadar city but remains hesitant to extend its presence inside the city owing to availability of cheaper and lower quality fuel. However, if Government takes action against this PSO will target Gwadar city to expand its retail network,
- Although annual revision of MS/HSD OMC margin with CPI remains intact, but PSO's management pointed out strong pursuance with concerned Ministries to ensure it is being granted persistently in the coming years.

Key Result highlights included:

- LPS income decline by 46%YoY to PKR 3.5bn owing to income received on overdue payment. However, the company expects to increase LPS income in FY18,
- Admin & marketing expense increased by +8%YoY owing to +5.5xYoY rise to PKR 511mn owing to increased marketing for lubes and other products,
- Owing to maturity of PIBs, loss of PIB income to be partially offset by continuation of LNG income,
- HSD sales remained flattish owing to increased competition as PSO's dealers obtained OMC license, however company plans to regain its market share through expansion in storage capacity and retail network,
- PSO to focus more on LPG and Lubricant business expansion and targets to become 1st and 2nd largest by 2020, respectively,

Exhibit: Highest ever core earnings in FY17 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 +7%YoY in FY17) is expected to further lift profitability as margins are de regulated and linked with price. The Company is expected to increase it storage capacity by 300k 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. Moreover, shelter to heavy inventory losses is expected to emanate from fortnightly revision in POL prices which was previously done on monthly basis. Furthermore, increased marketing and sales promotion for lubes should provide a healthy growth in the segment. Continuation of LNG business and increased volumes to partially offset decline in other income.

Recommendation

We maintain a **'BUY'** call on PSO with Dec-17 TP of PKR 519/share offering an upside of +14% from its last close. The company is currently trading at FY18E P/E of 6.3x and dividend yield of 4.8%. However, we will revisit our investment case once company's annual financial statements are available.

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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 priceon aforementioned security(ies) is in between -10% and 10%, from its last closing price(s)
Sell	If target price on aforementioned security(ies) is less than -10%, from its last closing price(s)

Time Horizon: Dec - 2017

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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