

Day Break

Friday, 21 October 2016

Company Update

Pakistan State Oil Co. Ltd.

Oil & Gas Marketing Companies

Recommendation	BUY
Target Price	491.7
Last Closing	416.8
Upside	18%

Market Data

Bloomberg Tkr.	PSO PA
Shares (mn)	271.7
Market Cap (PKRbn USDmn)	113.2 1,081.4
Exchange	KSE 100

Price Info.	90D	180D	365D
Abs. Return	1.5	18.6	28.5
Low	392.5	351.6	306.7
High	425.0	425.0	425.0

Key Company Financials

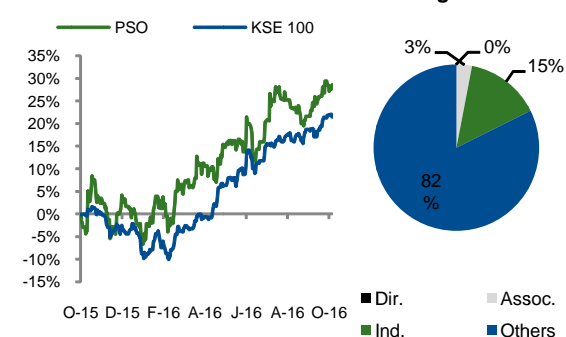
Period End: Jun

PKRbn	FY16A	FY17F	FY18F	FY19F
Total Revenue	678.0	807.1	912.0	1,036.7
Net Income	10.3	16.6	17.2	20.6
EPS (PKR)	37.8	61.2	63.2	76.0
DPS (PKR)	12.5	18.0	19.0	23.0
Total Assets	342.3	360.6	361.8	372.0
Total Equity	91.6	103.3	115.3	129.7

Key Financial Ratios

	FY16A	FY17F	FY18F	FY19F
ROE (%)	11%	16%	15%	16%
P/E (x)	11.0	6.8	6.6	5.5
P/B (x)	1.2	1.1	1.0	0.9
DY (%)	3.0	4.3	4.6	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: Higher Margin on MS/HSD and improved FO Sales to drive earnings in 1QFY17

- Pakistan State Oil's (PSO) board meeting is scheduled on 21st Oct-16, where we expect company to post earnings of PKR 4.4bn (EPS PKR 16.2) up by +35%YoY in 1QFY17
- We maintain our positive stance on PSO based on a) improved margins for MS and HSD with annual increase linked with CPI, b) normalized FO sales as Hub Plant resumes to standard operations, and c) recovery in FO prices to provide cushion for lost LNG income post Dec-16
- The scrip is currently trading at FY17F P/E of 6.8x. With our Jun-17 target price of PKR 492/share, the scrip offers +18% upside from its last closing price of PKR 417/share, hence we recommend a 'BUY' call on PSO.

Earnings to Clock in at PKR 16.2/share in 1QFY17

Pakistan State Oil's (PSO) board meeting is scheduled on 21st Oct-16, where we expect company to post earnings of PKR 4.4bn (EPS PKR 16.2) up by +35%YoY in 1QFY17 as compared to PKR 3.3bn (EPS PKR 11.9) in the same period last year. We attribute this accretion in profitability to a) increase in MS and HSD margins to PKR 2.41/ltr from previous PKR 2.35/ltr each, b) +31%YoY jump in FO volumes owing to higher demand from Hub plant post repair works on four boilers, and c) inventory gain of PKR 1.2bn as compared to inventory loss of PKR 12mn in the same period last year.

Exhibit: Financial Highlights

PKRmn	1QFY17E	1QFY16	YoY	4QFY16	MoM
Gross Sales	221,579	236,275	-6%	255,456	-13%
Net Sales	177,352	185,274	-4%	189,380	-6%
Gross Profit	8,764	7,545	16%	9,222	-5%
Operating Costs	3,704	3,349	11%	3,399	9%
Other Income	2,973	2,740	9%	5,870	-49%
EBIT	8,033	6,937	16%	11,694	-31%
Finance Cost	1,842	1,886	-2%	2,135	-14%
PBT	6,372	5,119	24%	9,558	-33%
PAT	4,397	3,252	35%	5,680	-23%
EPS (PKR)	16.18	11.97		20.90	
DPS (PKR)	-	-		7.50	

Source: IGI Research and Company Financials

Retail Product growth remains muted while FO sales jack up

PSO's retail product remained muted posting merely +4%YoY rise in MS volumes while HSD sales declined by 2%YoY during 1QFY17 likely owing to lack of expansion in retail outlets and scarcity of storage capacity. FO volumes picked up massively by +31%YoY, which in our view is mainly due to higher demand from Hub plant as repair work on boiler concluded in 2QFY16.

Exhibit: PSO Volumes

000'tons	1QFY17	1QFY16	YoY	4QFY16	MoM
MS	656	629	4%	654	0%
HSD	766	778	-2%	1,223	-37%
FO	2,050	1,559	31%	1,839	11%
Total	3,646	3,114	17%	3,877	-6%

Source: IGI Research and Company Financials

Outlook

We maintain our positive stance on PSO based on a) improved margins for MS and HSD with annual increase linked with CPI, b) normalized FO sales as Hub Plant resumes to standard operations, and c) recovery in FO prices to provide cushion for lost LNG income post Dec-16. It is pertinent to mention that circular debt remains prime risk to our valuation, however we anticipate no further accumulation based on Government's commitment to IMF to cap circular debt pile up. Although, as per media reports, recent hike in circular debt to level last seen back in 2013 is a matter of concern and therefore would again lead to liquidity concern for PSO. Moreover, possible shift of LNG contract from PSO to Pakistan LNG by Dec-16 would erode annual earnings by PKR 4-5/share (after tax).

Recommendation

The scrip is currently trading at FY17E P/E of 6.8x. With our Jun-17 target price of PKR 492/share, the scrip offers +18% upside from its last closing price of PKR 417/share, hence we recommend a **'BUY'** call on PSO.

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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)
Sell	If target price on aforementioned security(ies) is more than -10%, from its last closing price(s)

Time Horizon: Jun - 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 might unfavorably 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.

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