



AKD Securities Limited

TREC Holder & Registered Broker
Pakistan Stock Exchange

Equity Research / Pakistan

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Today's Daily

■ Downstream Oil: Forget quarterly CPI linkage of margins

With the half year line approaching, the OMC industry remains at fixed margins for retail fuels segment, where quarterly adjustment of margins to CPI remain elusive. Quarterly CPI-linkage of retail fuel margins was touted by the industry as a positive for earnings profile. While no official notification has enacted this mechanism, exercising caution over this mechanism for linkage of margins, we deliver a scenario analysis of the downstream oil space, highlighting incremental profitability and fair value addition in the case of a quarterly, half-yearly and annual CPI linkage of margins. HASCOL remains a prime beneficiary owing to its heavy reliance on retail fuels, followed by PSO and APL where their shares in HSD and MOGAS exposes them to upsides. With the de-regulation of the premium fuels segment, PSO's strong retail network is well placed for reaping the benefits of deregulation. At a FCFE based TP of PkR495/sh (assuming annual CPI indexation), offering 20% upside to last close, trading at FY17/18F PE of 8.7/7.2x and D/Y of 6%/7% underpins our BUY stance.

KSE100 - Index

Current 46,584.53
Previous 46,358.35
Chg. 0.49%

Mkt Cap. (PkRbn/US\$bn)

Current 9,333 / 89.04
Previous 9,303 / 88.75
Chg. 0.32%

Daily Turnover (mn)

Current 346.07
Previous 340.44
Chg. 1.7%

Value Traded (PkRmn/US\$mn)

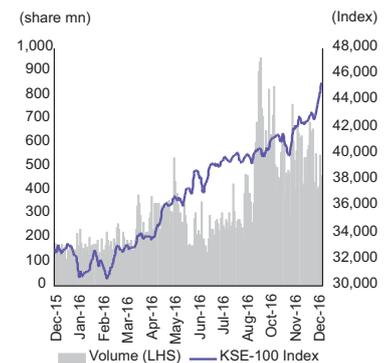
Current 19,494 / 185.98
Previous 19,364 / 184.74
Chg. 0.7%

AKD Daily

Monday, Dec 19, 2016

News and Views

- As per news report, The PSX will open the buying bids expressing interest in acquiring its 40% stake on Dec 22'16. At least 17 entities expressed interest in holding shares of the PSX.
- As per SNGPL, following a shortfall of 200 to 300MMCFD in the system, utility company has curtailed gas supply to a major fertilizer plant in Punjab to meet an increasing demand from domestic and commercial sectors.
- As per APCMA, the cement manufacturers have put their price increase plan on-hold in the hope that the GoP would consider reduction in duties on import of coal, amidst rising prices of coal in the international market.



Ali Asghar Poonawala
ali.poonawala@akdsecurities.net
111-253-111 Ext:646

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Downstream Oil: Forget quarterly CPI linkage of margins

With the half year line approaching, the OMC industry remains at fixed margins for retail fuels segment, where quarterly adjustment of margins to CPI remain elusive. Quarterly CPI-linkage of retail fuel margins was touted by the industry as a positive for earnings profile. While no official notification has enacted this mechanism, exercising caution over this mechanism for linkage of margins, we deliver a scenario analysis of the downstream oil space, highlighting incremental profitability and fair value addition in the case of a quarterly, half-yearly and annual CPI linkage of margins. HASCOL remains a prime beneficiary owing to its heavy reliance on retail fuels, followed by PSO and APL where their shares in HSD and MOGAS exposes them to upsides. With the de-regulation of the premium fuels segment, PSO's strong retail network is well placed for reaping the benefits of deregulation. At a FCFE based TP of PkR495/sh (assuming annual CPI indexation), offering 20% upside to last close, trading at FY17/18F PE of 8.7/7.2x and D/Y of 6%/7% underpins our BUY stance.

CPI indexation Scenarios: We highlight incremental profitability and fair value addition in the case of a quarterly, half-yearly and annual CPI linkage of margins. HASCOL remains a prime beneficiary owing to its heavy reliance on retail fuels (MS and HSD make up , followed by PSO and APL where their shares in HSD and MOGAS exposes them to upsides. Conversely, in the case for an annual CPI adjustment, PSO's earnings growth remains sustainable, exhibited by 4-YR earnings CAGR of 20% vs. 24.2/7.4% for HASCOL/APL. That said, we believe the laggard of this year's rally in OMC's, PSO remains attractive.

Scenario Analysis of CPI Indexation - HASCOL & PSO

HASCOL	CY17	% change over base	CY18	% change over base	CY19	% change over base	TP (PkR/sh.)
Quarterly	23.05	47%	41.44	119%	69.29	201%	785
Half Yearly	18.02	15%	25.55	35%	35.62	55%	469
Annual (Base Case)	15.71	-	18.94	-	23.03	-	312

PSO	FY17	% change over base	FY18	% change over base	FY19	% change over base	TP (PkR/sh.)
Quarterly	50.84	7%	75.41	31%	106.73	51%	874
Half Yearly	48.55	2%	62.91	9%	80.97	14%	596
Annual (Base Case)	47.48	-	57.49	-	70.76	-	495

Source: AKD Research & Co. Reports

Investment Perspective: With the de-regulation of the premium fuels segment, PSO's strong retail network is well placed for reaping the benefits of deregulation. Despite circular debt (receivables of PkR156bn due from power sector as of 1QFY17) and existing liquidity hurdles (receivables of PkR252bn growing 40%FYTD and at ~61% of total assets), better management of financial expenses, curtailment of borrowing costs by using accommodative facilities (collateralization of PIBs, FE-25) all the while focusing on expanding market share in the low receivables retail fuels segment. At a FCFE based TP of PkR495/sh (assuming annual CPI indexation), offering 20% upside to last close, trading at FY17/18F PE of 8.7/7.2x and D/Y of 6/7% underpins our BUY stance.

AKD Research CPI Projections

	FY17	FY18	FY19
Inflation Avg.	4.80%	6.10%	7%
	CY17	CY18	CY19
Inflation Avg.	5.80%	6.90%	7.10%

Source: AKD Research estimates



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