



## AKD Securities Limited

TREC Holder & Registered Broker  
Pakistan Stock Exchange

Equity Research / Pakistan



REP-108  
www.jamapunji.pk

### Today's Daily

#### ■ Macro swings are a boon for E&Ps

With expected cumulative YoY earnings growth of 31% in FY19, the recent round of currency devaluation coupled with interest rate hike is set to amplify the revenue stream of Pakistan's E&P sector going forward. OGDC/PPL/POL are currently trading at FY19F P/E of 6.28/7.05/8.00x, as compared to the sector's (3-yr avg.) historical P/E of 9.32x. Index heavyweights (OGDC and PPL) now offer capital upsides of 45.7/32.9% at our FY19/20F intl. oil assumptions of US\$70/65/bbl and long term forecast intact at US\$55/bbl. Significant contribution to PPL's and OGDC's bottom-lines also emanate from exchange gains. Moreover, higher interest rate environment provides additional return on bank deposits and other investments as E&P companies have historically remained cash rich with financial assets representing 24.4/25.4% of the total asset base in FY17/9MFY18. Having said this, we continue to push for OGDC and PPL, and while POL is trading below its fair value, we believe Jhandial's declining production and probability of dry wells cast concerns over its outlook, hence should be gradually offloaded as it derives ~40% of its value through this well only. Our FY19 TPs for OGDC/PPL/POL are PkR217/276/693/sh, respectively.

#### KSE100 - Index

Current 41,221.75  
Previous 41,795.59  
Chg. -1.37%

#### Mkt Cap. (PkRbn/US\$bn)

Current 8,476 / 65.97  
Previous 8,569 / 66.69  
Chg. -1.09%

#### Daily Turnover (mn)

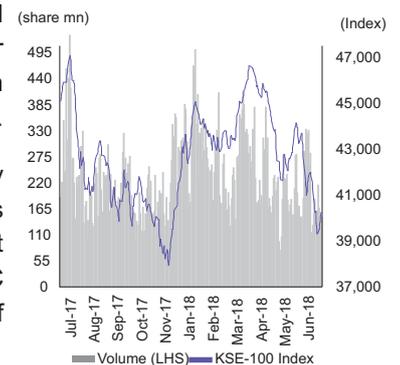
Current 222.68  
Previous 337.09  
Chg. -33.9%

#### Value Traded (PkRmn/US\$m)

Current 8,775 / 68.30  
Previous 13,090 / 101.87  
Chg. -33.0%

#### News and Views

- The economic managers are reportedly contemplating different options to raise the additional Customs Duty by 1% on all the imported items or to jack up the Regulatory Duty (RD) on 1,550 items to discourage the rising import bill. In this regard, the Ministry of Commerce and Federal Board of Revenue (FBR) held several meetings. In case of approval for raising additional Customs Duty by 1%, the exemption will remain available to some items such as medicines or raw materials.
- The Sindh High Court issued notices to Sui Southern Gas Company (SSGC) and Pakistan State Oil (PSO) on a petition of contract employees seeking regularization of their service. The petitioners submitted that they were contract employees working at different posts at the SSGC and the PSO and had already completed the prescribed period of probation.
- As per latest PBS data, textile exports rose around 9%YoY to US\$13.53bn for the fiscal year ended June 30'18 as financial incentives improved competitiveness of the key export-oriented sector. Category wise, knitwear exports increased 15.2%YoY to US\$2.71bn in FY18. Exports of bed-wear rose 5.8%YoY to US\$2.3bn while readymade garments exports fetched US\$2.6bn, up 11.22%YoY.



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**Impressive revenue growth to continue:** Despite stagnant volumetric output (Oil & Gas), AKD E&P Universe's revenue stream is expected to rise by 24.8%YoY in FY19F led by 22.7/24.1/40.3%YoY growth in OGDC/PPL/POL. Factors driving the rise include 1) ~20% avg. Pkr devaluation against the US\$ and 2) 13% jump in our assumed intl. oil price for FY19 vs 28% in FY18.

**Exchange gain is another item to cherish:** Movements in FX rates not only trigger top-line growth, but trickle down through other income as well. Refineries procure oil on credit from E&P companies, leaving a net asset exposure where the lag in payment effectively translates into exchange gains for these companies. This item is expected to add Pkr0.42/1.33/3.43sh towards OGDC/PPL/POL's EPS projection for FY19F. However, owing to its accounting policy, POL records a subsequent exchange loss on US\$ denominated "provision for decommissioning cost" (and thereby nullifies the exchange gain) while PPL and OGDC gradually amortise the corresponding capitalized asset entry over a longer period, effectively gaining from Pkr devaluations.

**Leveraging the cash rich balance sheet:** Cash, bank balance and investments effectively represent 26.6/22.1/31.8% of OGDC/PPL/POL's 9MFY18 overall assets. In this purview, hike in interest rates creates another opportunity for bottom-line accretion as return on investment rises. We have assumed OGDC to reinvest the TFC proceeds in high yielding long term government certificates, while PPL and POL should

### EPS Sensitivity to (Pkr/sh)

	+US\$5/bbl movement in oil price	Pkr devaluation of +5%
OGDC	1.43	1.35
PPL	1.37	1.41
POL	4.56	3.61

Source: AKD Research



get higher returns on TDRs translating into other incomes of PkR2.32/2.52/2.35/sh for FY19F. We believe liquid returns from this head can easily be paid out as cash dividends even in the case of outstanding receivables (especially for OGDC).

**Investment Perspective:** Incorporating our revised assumptions, OGDC/PPL/POL's EPS estimates stand at PkR23.5/29.45/78.72/sh for FY19F. Recent changes in Pakistan macro assumptions have been a blessing for the sector, and valuations have become more attractive. At current levels, OGDC is our best pick with a capital upside of 45.7%, while PPL follows with 32.9% upside potential. POL, however, is trading at a premium as compared to its counterparts despite i) hydrocarbon flows from Jhandial being reduced to 1/3rd of its original (where Jhandial makes up ~40% of POL's value) and ii) industry sources indicating no economic benefit of the ongoing exploration wells, hence we believe should be gradually offloaded in the current scenario despite trading at less than its fair value.



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Accumulate	> 5% to < 20% upside potential
Neutral	≤ 5% to ≥ -5% potential
Reduce	< -5% to > -20% downside potential
Sell	≤ -20% downside potential



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