

## Company Update

### Pakistan State Oil Co. Ltd.

Oil & Gas Marketing Companies

<b>Recommendation</b>	<b>BUY</b>
Target Price	489.1
Last Closing	335.5
Upside	46%

#### Market Data

Bloomberg Tkr.	PSO PA
Shares (mn)	271.7
Market Cap (PKRbn   USDmn)	91.1   870.5

#### Price Info.

	90D	180D	365D
Abs. Return	(1.1)	(5.4)	(14.8)
Low	306.7	287.0	287.0
High	342.2	356.1	404.1

#### Key Company Financials

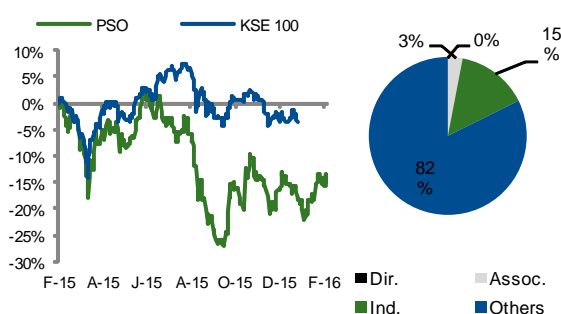
Period End: Jun

PKRbn	FY15A	FY16E	FY17F	FY18F
Total Revenue	913.1	724.7	800.5	862.2
Net Income	6.9	13.0	14.7	16.1
EPS (PKR)	25.5	47.7	54.3	59.1
DPS (PKR)	10.0	12.0	14.0	15.0
Total Assets	341.3	301.3	318.9	338.4
Total Equity	82.3	92.0	103.0	114.9

#### Key Financial Ratios

ROE (%)	8%	14%	14%	14%
P/E (x)	13.1	7.0	6.2	5.7
P/B (x)	1.1	1.0	0.9	0.8
DY (%)	3.0	3.6	4.2	4.5

#### 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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## Pakistan State Oil

### Hefty Volumes Driving +57%YoY growth in Earnings in 1HFY16

- PSO posted earnings of PKR 3.5bn (EPS PKR 12.78) in 2QFY16 compared to a loss of PKR 0.96bn (LPS PKR 3.53) in the same period last year. Along with the result, company announced a cash dividend of PKR 5.0/share.
- Continuing the declining trend, PSO again lost significant market share in Jan-16 to 35% as compared to 41% in Dec-15, which in our view is likely due to lack of expansion in retail outlets owing to cash flow constraints. With no accumulation in receivables and better cash flow position for PSO, we believe company can now expand its retail outlets (already in process) to gain its lost market share to other OMCs, which are actively expanding their retail outlets such as HASCOL, APL and SHEL.
- We currently have a strong **“BUY”** call on PSO with our Dec-16 TP of PKR 489/share, offering +46% upside from its last closing of PKR 335/share. PSO is currently trading at a FY16 P/E and P/B of 7.0x and 1.0x, respectively.

#### Earnings for 2QFY16 clocked in at PKR 12.78/share, DPS PKR 5.00

Pakistan State Oil Company (PSO) posted earnings of PKR 3.5bn (EPS PKR 12.78) in 2QFY16 compared to a loss of PKR 0.96bn (LPS PKR 3.53) in the same period last year. Cumulative earnings for 1HFY16 clocked in at PKR 6.7bn (EPS PKR 24.76) depicting a growth of +57%YoY compared to PKR 4.3bn (EPS PKR 15.77) in the corresponding period.

Along with the result, company announced a cash dividend of PKR 5.0/share.

#### Volumes Driving Earning Growth

The growth in earnings during 2QFY16 is attributed to +15%YoY growth in overall volumes led by +15% / 9% / 18%YoY jump in MS / HSD / FO volumes to 0.58 / 0.93 / 1.35mnTon, respectively. FO contribution to profit declined by 43%YoY to PKR 1.08bn in 1HFY16, owing to 41%YoY drop in FO prices and 3%YoY decline in volumetric sales.

**Exhibit: PSO Volumes**

	2QFY16	2QFY15	YoY	1HFY16	1HFY15	YoY
MS	582	505	15%	1,211	963	26%
HSD	933	859	9%	1,710	1,683	2%
FO	1,354	1,145	18%	2,914	2,994	-3%
Total	3,035	2,650	15%	6,149	5,912	4%

Source: IGI Research and Company Financials

**Lower Inventory loss during 1HFY16**

PSO booked inventory loss of PKR 0.6bn in 1HFY16 as compared to PKR 1.8bn in 1HFY15. The company was able to book inventory gains on MS and FO to the tune of PKR 2.0bn and PKR 1.6bn, respectively but higher inventory loss of HSD of PKR 4.0bn due to 54 days of inventory level, resulted in a net inventory loss. During the period, PSO maintained 13 days and 12 days of inventory for MS and FO, respectively.

**Exhibit: Financial Highlights**

PKRmn	2QFY16	2QFY15	YoY	1HFY16	1HFY15	YoY
Gross Sales	227,094	259,987	-13%	463,370	604,569	-23%
Net Sales	168,691	217,853	-23%	353,965	508,287	-30%
Gross Profit	6,616	894	640%	14,161	12,508	13%
Operating Expenses	2,908	3,412	-15%	6,257	7,783	-20%
Other operating Income	2,564	3,349	-23%	5,304	6,722	-21%
EBIT	6,272	830	655%	13,209	11,446	15%
Finance Cost	1,715	3,267	-48%	3,601	5,941	-39%
Profit Before Taxation	4,878	(2,314)	N/M	9,996	5,529	81%
Profit After Taxation	3,473	(960)	N/M	6,726	4,283	57%
EPS (PKR)	12.78	(3.53)		24.76	15.77	
DPS (PKR)	5.00	-		5.00	-	

Source: IGI Research and Company Financials

**Other Expenses and Finance Cost supporting Profitability**

Other expenses declined by 20%YoY (15%YoY in 2QFY16) in 1HFY16 to PKR 6.3bn which as per management is due to reversal of PKR 0.2bn bad debt provision, as compared to PKR 0.8bn provisioning charge made in same period last year. Finance cost decreased by 39%YoY (48%YoY in 2QFY16) owing to lower mark up rates and smaller overdraft balance. Other income declined by 21%YoY (down by 23%YoY in 2QFY16), which as per management is on the back of lower penal interest due to timely payments by power sector and lesser LPS payment from PIA (PKR0.9bn in 1HFY16 versus PKR 1.8bn in 1HFY15)

**No Accumulation in Receivables from Power Sector**

PSO's overall receivables have declined by 7% to PKR 170bn during 1HFY16 mainly due to 10% drop in receivables from power sector to PKR 137bn since Jun-15. This has led to lower short term borrowing requirement and better cash flow position for the company.

**Exhibit: PSO Receivables**

PKR	Feb-16	Dec-15	Jun-15
Power sector	137	137	152
LNG (SNGP)	9	11	8
Price Diff claims from GoP	9	9	10
PIA	13	13	13
Total	168	170	183

Source: IGI Research and Company Financials

**Outlook**

Continuing the declining trend, PSO again lost significant market share in Jan-16 to 35% as compared to 41% in Dec-15, which in our view is likely due to lack of expansion in retail outlets owing to cash flow constraints. With no accumulation in receivables and better cash flow position for PSO, we believe company can now expand its retail outlets (already in process) to gain its lost market share to other OMCs, which are actively expanding their retail outlets such as HASCOL, APL and SHEL.

**Recommendation**

We currently have a strong **“BUY”** call on PSO with our Dec-16 TP of PKR 489/share, offering +46% upside from its last closing of PKR 335/share. PSO is currently trading at a FY16 P/E and P/B of 7.0x and 1.0x, respectively.

### Analyst Certification

The analyst<sup>^</sup> hereby certify that the views about the company/companies and the security/securities discussed in this report are accurately expressed and that he/she has not received and will not receive direct or indirect compensation in exchange for expressing specific recommendations or views in this report. The analyst is principally responsible for the preparation of this research report and that he/she or his/her close family/relative does not own 1% or more of a class of common equity securities of the following company/companies covered in this report.

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Recommendation	Rating System
Buy	If return on aforementioned security(ies) is more than 10%, from its last closing price(s)
Hold	If return on aforementioned security(ies) is in between -10% and 10%, from its last closing price(s)
Sell	If return on aforementioned security(ies) is more than -10%, from its last closing price(s)

### Valuation Methodology

The analyst<sup>^</sup> has used following valuation methodology to arrive at the target price of the said security (ies):

- DCF(Discounted Cash Flow)

#### Time Horizon

- Dec - 2016

#### Risk

- Changes in State Bank of Pakistan Policy Rate
- Changes in exchange rate
- Changes in Circular Debt quantum

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