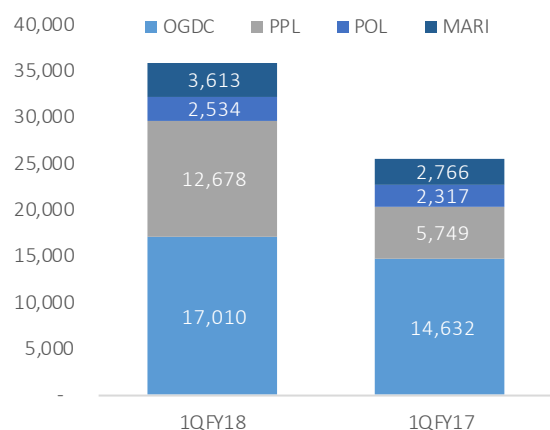


# Day Break

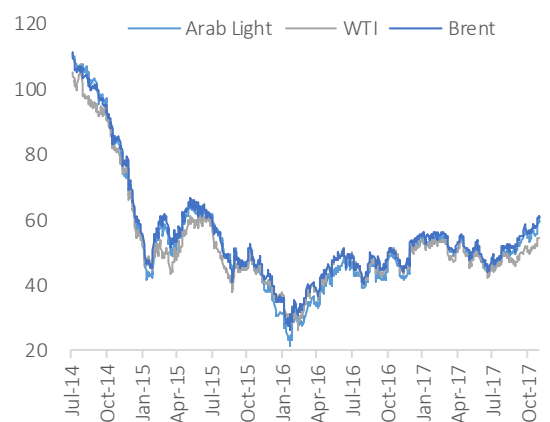
Tuesday, 07 November 2017

## Sector Update

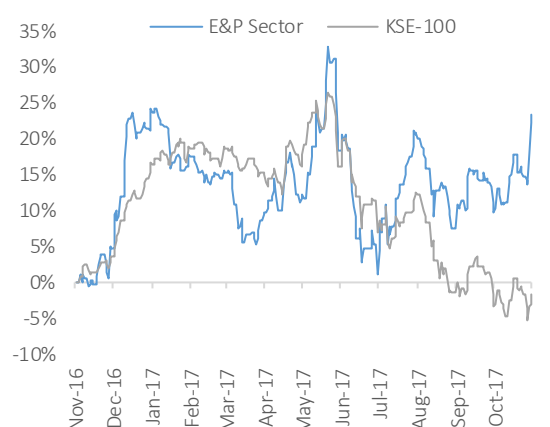
E&P Sector Profitability for 1QFY18 - (PKRmn)



Crude Oil historical prices - (USD/bbl)



Relative Performance to KSE 100



Source: Bloomberg, PSX & IGI Research

### Analyst

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## Oil & Gas – Exploration Companies

### E&P sector back in limelight; rising oil prices puts cherry on top, MARI and PPL top picks

- Oil prices have started to rise with Arab Light price (benchmark crude), up by nearly +30% since FY18 to date, as geopolitical tension in Middle East rises along with US oil inventory and rig count witnessing a steady decline.
- IGI E&P universe has gained +19% in FY18TD on the back of nearly 30% hike in oil prices and one-off impact in respect of notification of revision in wellhead prices for Tal block (only for PPL/POL/OGDC)
- It is pertinent to mention here that POL remains most sensitive to changes in oil prices in terms of EPS and target price. We highlight, that for every USD 1/bbl increase in oil price POL, PPL, MARI and OGDC EPS will augment by +1.7%, +1.4%, +1.1% and +0.9%, respectively.
- We have revised upwards our target price for OGDC, PPL and POL by +0.5%, +2.0% and +2.7% after incorporating recent discovery of Makori East-06 in Tal block. Our target prices for MARI, PPL, OGDC and POL stand at PKR 2,209/share, PKR 212/share, PKR 180/share and PKR 645/share, respectively. We highlight PPL and MARI as our preferred picks in IGI E&P universe.

#### Oil price down by 30% in FY18TD as oil market tightens...

Oil prices have started to rise with Arab Light price (benchmark crude), up by nearly +30% since FY18 to date, as geopolitical tension in Middle East rises along with US oil inventory (down by 10% in FY18TD) and rig count witnessing a steady decline (down to 729 rigs in Oct-17 from 768 in Aug-17). More recent, key members of Saudi Arabia ministry were arrested on corruption charges leading to country wide anti-corruption movement. On the demand side, China world largest oil consumer has shown improving growth trend leading to higher oil consumption. To top it up, OPEC upcoming meeting schedule on 30<sup>th</sup> Nov-17, is expected to extend production cuts beyond Mar-18 by both OPEC and Non-OPEC members.

#### ...leading to a +19% return in IGI E&P universe in FY18TD

IGI E&P universe has gained +19% in FY18TD on the back of nearly 30% hike in oil prices and one-off impact in respect of notification of revision in wellhead prices for Tal block (only for PPL/POL/OGDC). However, on individual basis company specific factors also corroborated the price rally alongside oil prices, +41%YoY rise in sector profitability and Tal block impact. POL leads the pack with highest return of +38% in FY18TD which was primarily backed by significant discovery in Jhandial-01, followed by PPL posting 33% in FY18TD on account of higher wellhead price for Sui field effective from FY18 and reversal of amount relating to transfer of 50% working interest in Kotri North to UEPL. OGDC has so far recorded a return of +15% in FY18TD as KPD-TAY project commenced production from Sep-17. However, MARI return is down by 2% in FY18TD as Government of Pakistan (GoP) pushes for divestment of stake in MARI despite a +31%YoY rise in earnings in 1QFY18.

**Our long-term oil price assumption stands at USD 50/bbl**

Our long-term oil price assumption stands at USD 50/bbl and while oil prices are currently trading USD 59.8/bbl (averaging USD 52.03/bbl in FY18TD), we expect oil prices to average between USD 50-55/bbl for FY18. However, we still maintain our long-term price assumption of USD 50/bbl as future contracts for oil prices are currently trading at USD 49-52/bbl beyond FY20 for WTI which currently stands at USD 57.36/bbl.

Exhibit:  
**U.S inventory down by 10% in FY18TD**

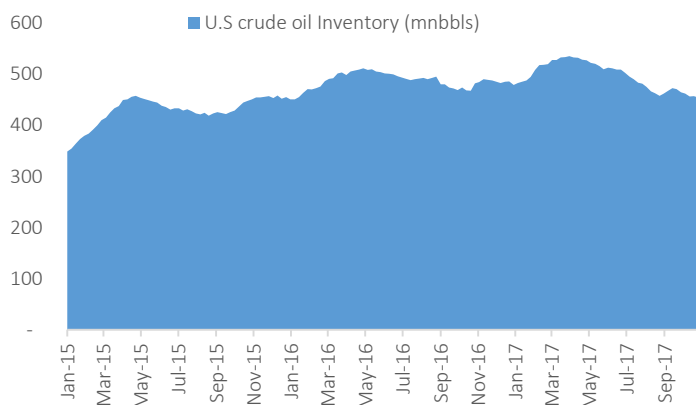
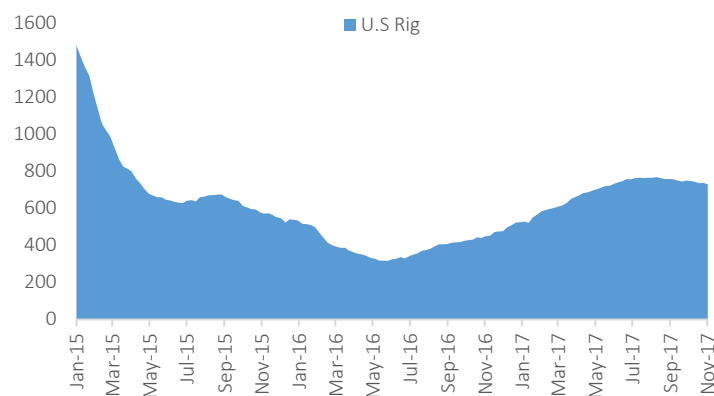


Exhibit:  
**US rig count on a decline since Jul-17, lowest level since May-16**



Source: IGI Research, Company Financials, Bloomberg

**Sensitivity of EPS to changes in oil prices**

Oil price (Arab Light) is currently averaging USD 52.03/bbl for FY18TD. For oil prices to average between USD 55-60/bbl, a level of USD 60-65/bbl will have to persist for the remaining part of FY18. As the oil prices are currently trading above our price assumption, we provide a sensitivity of change in oil prices to EPS and target price company-wise. It is pertinent to mention here that POL remains most sensitive to changes in oil prices in terms of EPS and target price, as oil revenues contribute nearly 42% of total revenue for POL compared to 34%, 26% and 10% for OGDC, PPL and MARI, respectively. We highlight, that for every USD 1/bbl increase in oil price POL, PPL, MARI and OGDC EPS will augment by +1.7%, +1.4%, +1.1% and +0.9%, respectively.

Exhibit:  
**P/E and 3Yr EPS CAGR comparison**

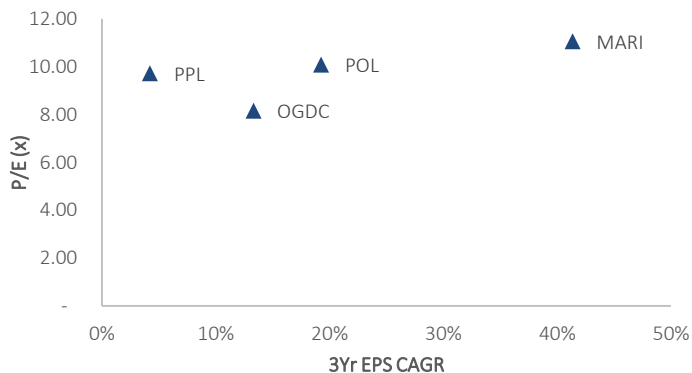
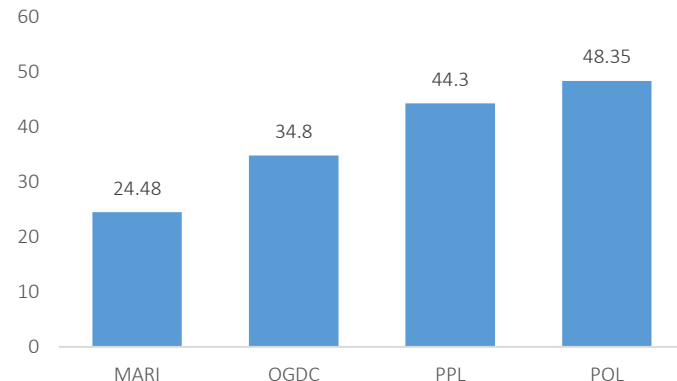


Exhibit:  
**MARI trading at lowest implied oil price, while POL trading at highest – (USD/bbl)**



Source: IGI Research, Company Financials

### PPL and MARI as our top picks

We have revised upwards our target price for OGDC, PPL and POL by +0.5%, +2.0% and +2.7% after incorporating recent discovery of Makori East-06 in Tal block. Our target prices for MARI, PPL, OGDC and POL stand at PKR 2,209/share, PKR 212/share, PKR 180/share and PKR 645/share, respectively. We highlight PPL and MARI as our preferred picks in IGI E&P universe. PPL and MARI are currently trading at FY18F P/E of 9.7x and 11.1x respectively, however MARI offers the highest 3Yr earnings CAGR of +41%.

## EPS and target price sensitivity for IGI E&P Universe for change in oil prices

### POL EPS and target price sensitivity

Scenarios	Oil Assumption (USD/bbl)			EPS (PKR)			Target Price (PKR) - Jun'18
	FY18	FY19	FY20	FY18	FY19	FY20	
Bear	45.0	45.0	45.0	58.2	63.5	63.2	605.1
Base	50.0	50.0	50.0	63.3	70.0	69.4	644.8
Bull 1	55.0	55.0	55.0	68.2	76.0	75.2	681.1
Bull 2	60.0	60.0	60.0	73.0	82.0	80.9	717.3

Source: IGI Research

### PPL EPS and target price sensitivity

Scenarios	Oil Assumption (USD/bbl)			EPS (PKR)			Target Price (PKR) - Jun'18
	FY18	FY19	FY20	FY18	FY19	FY20	
Bear	45.0	45.0	45.0	18.7	19.4	18.5	199.2
Base	50.0	50.0	50.0	20.4	21.4	20.5	212.4
Bull 1	55.0	55.0	55.0	21.9	23.1	22.1	223.2
Bull 2	60.0	60.0	60.0	23.3	24.7	23.8	234.0

Source: IGI Research

### MARI EPS and target price sensitivity

Scenarios	Oil Assumption (USD/bbl)			EPS (PKR)			Target Price (PKR) - Jun'18
	FY18	FY19	FY20	FY18	FY19	FY20	
Bear	45.0	45.0	45.0	131.4	180.3	218.8	2,095.6
Base	50.0	50.0	50.0	140.2	192.8	234.1	2,208.9
Bull 1	55.0	55.0	55.0	147.8	203.0	246.2	2,297.4
Bull 2	60.0	60.0	60.0	155.3	213.2	258.3	2,385.9

Source: IGI Research

### OGDC EPS and target price sensitivity

Scenarios	Oil Assumption (USD/bbl)			EPS (PKR)			Target Price (PKR) - Jun'18
	FY18	FY19	FY20	FY18	FY19	FY20	
Bear	45.0	45.0	45.0	19.0	21.8	20.6	173.8
Base	50.0	50.0	50.0	19.9	22.9	21.6	179.5
Bull 1	55.0	55.0	55.0	20.7	23.8	22.5	184.8
Bull 2	60.0	60.0	60.0	21.6	24.8	23.4	190.2

Source: IGI Research

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**Time Horizon:** Jun – 2018

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