

Day Break

Friday, 13 October 2017

COMPANY UPDATE

PAKISTAN OILFIELDS LIMITED OIL & GAS EXPLORATION COMPANIES

Recommendation	BUY
Target Price:	619.7
Last Closing: 12-Oct-17	552.8
Upside:	12.1
Valuation Methodology:	Reserve based - Discounted Cash Flow (DCF)
Time Horizon:	Jun-18

Market Data

Bloomberg Tkr.	POL PA
Shares (mn)	236.5
Free Float Shares (mn)	108.3
Free Float Shares (%)	45.8%
Market Cap (PKRbn USDmn)	130.8 1,241.8
Exchange	KSE 100
Price Info.	90D 180D 365D
Abs. Return	22.5 14.8 26.6
Lo	429.8 429.8 396.5
Hi	541.2 541.2 559.6

Key Company Financials

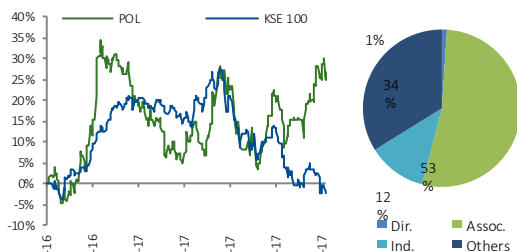
Period End: Jun

PKRbn	FY16A	FY17A	FY18E	FY19F
Total Revenue	24.8	27.3	35.4	41.4
Net Income	7.23	9.7	13.0	15.9
EPS (PKR)	30.6	40.9	54.9	67.1
DPS (PKR)	35.0	40.0	50.0	65.0
Total Assets	55.7	57.7	68.6	75.2
Total Equity	30.2	31.5	32.7	33.2

Key Financial Ratios

ROE (%)	24.0	30.7	39.8	47.9
P/E (x)	18.1	13.5	10.1	8.2
P/B (x)	4.3	4.2	4.0	3.9
DY (%)	6.3	7.2	9.0	11.8

Relative Price Performance & Shareholding



About the Company

The Company is incorporated in Pakistan as a public limited company. The Company is principally engaged in exploration, drilling and production of crude oil and gas. The Company is a subsidiary of the Attock Oil Company Limited, UK and its ultimate parent is Bay View International Group, S.A.

Source: Bloomberg, PSX & IGI Research

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Oil & Gas – Exploration Companies

Jhandial to up POL's earnings, arresting sustainability concerns

- We have revised our investment case for Pakistan Oilfields Limited (POL) on the back of recent discovery from exploratory well Jhandial-1 in Ikhlas block.
- We have also incorporated the full year FY17 financial statements.
- Considering the actual flows vary from initial tests, we have assumed moderate flows of 2,160bopd/19mmcf of oil/gas production at an average reserve life of 9 years for oil and 11 years for gas. Based on this, we have estimated annualized earnings impact of PKR 9.70/share at an oil price assumption of USD 50/bbl.
- We maintain our "BUY" call on POL with our revised Jun-18 target price of PKR 620/share (up by +15% from previous PKR 540/share), offering +12% upside from its last closing. The company is currently trading at a FY18E P/E of 10.1x and offers a healthy dividend yield of 9.0%.

Earnings revised upwards; Jhandial discovery to arrest POL's earnings sustainability concern

We have revised our investment case for Pakistan Oilfields Limited (POL) on the back of recent discovery from exploratory well Jhandial-1 in Ikhlas block. We have also incorporated the full year FY17 financial statements. As a result our earnings estimates for FY18/19/20F have been revised upwards by 18%-22% leading to an increase in our Jun-18 target price by +15% to PKR 620/share (previous PKR 540/share).

Discovery from Jhandial-1 in Ikhlas to hold significant value addition for POL

To recall, in a recent PSX filing on 4th Oct-17 POL announced a substantial hydrocarbon discovery from its exploratory well Jhandial-1 in Ikhlas block which is operated by POL with a post-commercial working interest of 80%. The discovery fetched flow rates at 3 different choke sizes. This discovery will be priced under Petroleum Policy 2012 (PP12) which offers a +67% higher gas price compared to PP01. Ikhlas block lies in KPK which lies in the region of Khaur, Pariwali, Dhok Sultan, Ratana, Dhulian and Meyal where average reserve size stood between 1-43mnbbls however, since 1989 the discovery size stands between 1-9mnbbls.

Exhibit:

Discovery Size at Different choke size and PSI

Choke Size	Pressure (PSI)	Oil (bopd)	Gas (mmcf)
40/64"	3,768	2,520	21
32/64"	5,364	2,160	19
28/64"	6,290	1,630	17

Source: IGI Research, PSX

Assuming an average 2,160bopd/19mmcf of oil/gas production...

Considering the actual flows vary from initial tests, we have assumed moderate flows of 2,160bopd/19mmcf of oil/gas production at an average reserve life of 9 years for oil and 11 years for gas resulting in likely reserves of 6.8mnbbls and 80bcf

of gas reserves, respectively. Our assumption stands contrary to reserve figures quoted by newspaper citing recently. We base our assumption on recent discoveries made in the region surrounding Ikhlas block where the discovery size since 1989 has been in the range of 1.1-9.0mnbbls.

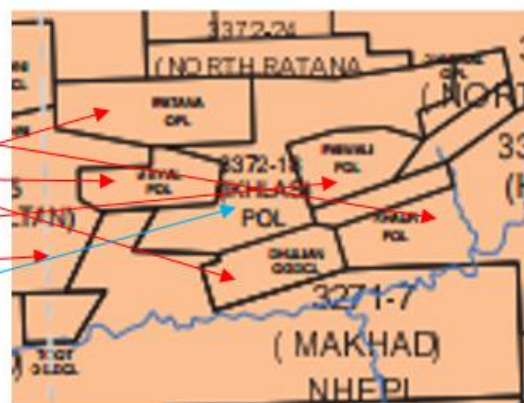
Exhibit:

Estimated Reserve size based on different flow rates

Case	Choke Size	Oil	Reserve Life	Total Reserve Size (mnbbl)	Gas	Reserve Life	Total Reserve Size (BCF)
	40 / 64"	2,520	9	8.28	21.0	11	84.3
Base Case	32 / 64"	2,160	9	7.10	19.0	11	76.3
	28 / 64"	1,630	9	5.35	16.5	11	66.2

Recent discoveries along Ikhlas Block had lesser reserves compared to older discoveries

	Year	mnbbls		
		Original	Cumulative	Balance
Khaur	1915	4.3	4.2	0.1
Dhulian	1937	42.9	42.4	0.5
Meyal	1968	42.8	42.0	0.8
Ratana (Cond)	1989	5.9	2.9	3.0
Pariwali	1994	9.0	8.4	0.6
Dhok Sultan	2015	1.1	-	1.1
Region Average		17.6	16.6	1.0
Ikhlas	2017			



Source: IGI Research, PPIS, Company Financial, PSX

...we estimate earnings impact of PKR 9.7/share

Based on this, we have estimated annualized earnings impact of PKR 9.70/share at an oil price assumption of USD 50/bbl. However at maximum production flows stated by POLs management of 2,520bopd for oil and 21mmcf for gas, we estimate annualized earnings impact of PKR 11.1/share.

Exhibit:

Jhandial -1 well, Net Income impact from Oil and Gas flows at different choke sizes

Case	Arab Light (USD/bbl)	Oil Flows (Bopd)	Net Income from Oil Flows (PKRmn) - A	Gas Price (PKR /mmbtu)	Heating Value (mmbtu)	Gas Flows (mmcf)	Net Income from Gas	Total net income = A+B (PKRmn)	Total net income = A+B (PKR/share)
							Flows (PKRmn) - B		
	50	2,520	1,352	508	1,161	21.0	1,266	2,619	11.1
Base Case	50	2,160	1,159	508	1,161	19.0	1,146	2,305	9.7
	50	1,630	875	508	1,161	16.5	995	1,870	7.9

Source: IGI Research, PPIS, PSX, Company Financials

Exhibit:
Estimated oil reserves for POL to go up by nearly ~+30% after inclusion of Jhandial

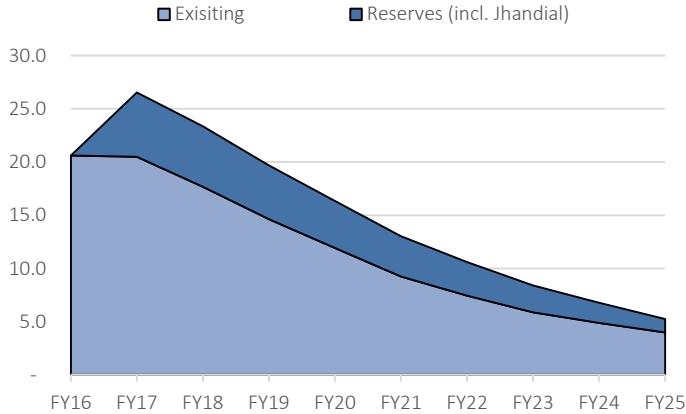
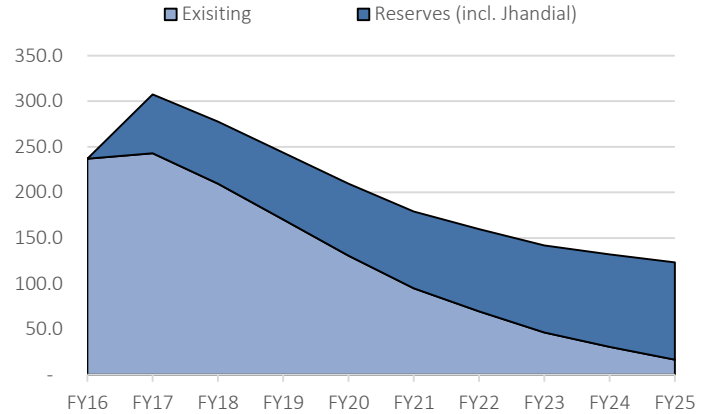


Exhibit:
Estimated Gas reserves for POL to go up by nearly ~+26% after inclusion of Jhandial



Source: IGI Research, PPIs, Company Financial, PSX

Even at 23mnbbls earnings impact should remain marginal while average reserve life may expand beyond 9 years

In our view, probability of a high oil and gas reserve base for Jhandial remains remote, but nevertheless we highlight that if reserves figure (to be reported by POL) turns out to be higher than our estimates, the impact will increase both 1) reserve life and our 2) target price however, earnings impact will remain the same. That said, if Jhandial reserves turn out to be substantial increased reserve life would provide extended sustainability of earnings for the company. POL’s current oil and Gas reserves stand at 20.5mnbbls and 243bcf, respectively with an estimated reserve life of 7.9 years. However, after inclusion of Jhandial reserves we estimate POL’s total reserves life to expand beyond 9 years.

Earnings to grow by +34%YoY in FY18 on the back of improved production...

We expect POLs earnings to grow by +34%YoY in FY18 and post 3Yr earnings CAGR of 18% over FY18-20F. This is on the back of a) stable oil prices with possible rise on the back of easing global oil supply and demand, b) oil and gas production to increase by +29%/+17%YoY in FY18 on the back of full year impact of Mardankhel, production commencement from Makori Deep and flows from Jhandial, and c) PP12 pricing on new production from Jhandial and Makori Deep.

...while recovery in oil prices and PKR devaluation remain key upside triggers

Besides production enhancement, other key catalyst for earnings growth are recovery in oil prices and PKR devaluation. We highlight that every USD 1/bbl increase in oil prices lifts our earnings forecast by +2% and every 1% PKR devaluation has 1% - 1.5% incremental impact on earnings.

Recommendation

We maintain our **“BUY”** call on POL with our revised Jun-18 target price of PKR 620/share (up by +15% from previous PKR 540/share), offering +12% upside from its last closing. The company is currently trading at a FY18E P/E of 10.1x and offers a healthy dividend yield of 9.0%.

Earnings and target price sensitivity to changes in oil price and exchange rate

Exhibit:

EPS and Target Price Sensitivity to Oil Prices

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	49.9	60.9	60.6	581.5
Base	50.0	50.0	50.0	54.9	67.1	66.5	619.7
Bull 1	55.0	55.0	55.0	59.7	72.9	72.0	654.5
Bull 2	60.0	60.0	60.0	64.5	78.6	77.5	689.4
Bull 3	65.0	65.0	65.0	69.3	84.4	83.0	724.2

Source: IGI Research

Exhibit:

EPS and Target Price Sensitivity to Change in exchange rate

Scenarios	PKR/USD	Change	EPS	Change	Target Price (PKR) - Jun-18	Change
	FY18	%	FY18	%		%
Bear	105.24	-2%	53.51	-3%	609.07	-2%
Base	107.38	0%	54.94	0%	619.66	0%
Bull 1	109.53	2%	56.38	3%	630.25	2%
Bull 2	111.68	4%	57.82	5%	640.84	3%
Bull 3	113.83	6%	59.25	8%	651.43	5%

Source: IGI Research

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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 less than -10%, from its last closing price(s)

Time Horizon: Jun – 2018

Valuation Methodology: The analyst(s) has used following valuation methodology to arrive at the target price of the said security (ies):

(Reserve Based DCF Valuation)

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Basic Definitions and Terminologies used: **Target Price:** A price target is the projected price level of a financial security stated by an investment analyst or advisor. It represents a security's price that, if achieved, results in a trader recognizing the best possible outcome for his investment. **Market Cap.:** Market capitalization is calculated by multiplying a company's shares outstanding by current trading price. **ROE:** Return on equity is the amount of net income returned as a percentage of shareholders' equity. **P/E:** Price to Earnings ratio of a company's share price to its per-share earnings. **P/B:** Price to Book ratio used to compare a stock's market value to its book value. **DY:** The dividend yield is dividend per share, divided by the price per share.

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