Detailed Report

Wednesday, 20 September 2017

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DETAILED REPORT

HASCOL PETROLEUM LIMITED
OIL & GAS MARKETING COMPANIES

Recommendation		BUY
Target Price:		389.4
Last Closing:	19-Sep-17	287.5
Upside:		35.4
Valuation Methodology:		Discounted Cash Flow (DCF)
Time Horizon:		Dec-17

Market Data

Bloomberg Tkr.		HASCOL PA
Shares (mn)		120.7
Free Float Shares (mn)		60.3
Free Float Shares (%)		50.0%
Market Cap (PKRbn | USDmn)	34.7	330.0
Exchange		KSE 100

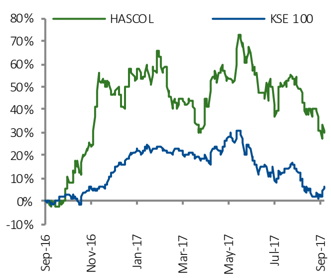
Price Info.	90D	180D	365D
Abs. Return	(16.4)	(9.0)	29.8
Lo	286.1	286.1	219.9
Hi	352.0	389.4	389.4

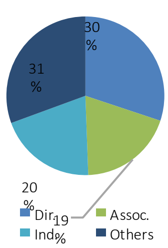
Key Company Financials

Period End: Dec

PKRbn	CY16A	CY17E	CY18F	CY19F
Total Revenue	99.5	136.8	153.7	174.6
Net Income	1.22	1.7	2.0	2.6
EPS (PKR)	10.1	13.8	16.6	21.2
DPS (PKR)	7.0	8.0	9.0	12.0
Total Assets	44.6	54.7	58.7	65.5
Total Equity	6.1	6.8	7.6	8.8
Key Financial Ratios				
ROE (%)	19.9	24.7	26.2	29.2
P/E (x)	28.5	20.8	17.3	13.6
P/B (x)	5.7	5.1	4.5	4.0
DY (%)	2.4	2.8	3.1	4.2

Relative Price Performance & Shareholding





About the Company

The principal activities of the Company are procurement, storage and marketing of petroleum and related products. Company is involved in marketing and distribution of (Mogas), HSD, FO, Jet Fuel (JP-1), Kerosene, CNG, LPG, Petrochemicals and Lubricants.

Source: Bloomberg, PSX & IGI Research

Abdullah Farhan
Research Analyst
Abdullah.farhan@igi.com.pk
Tel: (+92-21) 111-234-234 Ext.: 912

Hascol Petroleum Limited

Earnings revised down; 'Buy' rating intact as double digit earnings growth to drive valuation

CY17 earnings estimates revised down to PKR 13.8/share; reflecting higher tax liability, delays in OMC margins and higher operating expense

We have revised down our earnings estimates for Hascol Petroleum Limited (HASCOL) to PKR 13.83/share / PKR 16.59/share / PKR 21.19/share (down by 19%/30%/32%) for CY17E/18F/19F. We base our earnings revision on the back of a) higher tax rate owing to standing deferred tax liabilities in CY17, b) higher selling and distribution costs as company gears up its advertisement and promotional expense, and finally c) delays in OMC margin increase for MS and HSD for FY18. As a result, we have revised down our target price for HASCOL to PKR 389.41/share (down by 9%) from previous PKR 430/share.

However, 'Buy' rating intact as double digit earnings growth to drive valuation

Despite aforementioned factors, we estimate double digit earnings growth story to continue, posting a 3Yr forward CAGR of +26%. The company has stepped up its expansion plans focusing around CPEC route targeting both retail outlets and storage capacities. With these initiatives, the company will not only be able to post above industry growth but would also be able to capture additional market share. As a result we estimate HASCOL volumes to register +25% growth in the next three years with MS leading the volume chart leading to increased market share from current ~9% in CY16 to ~12% by CY19. In addition, margins accretion of MS and HSD linked with CPI inflation and normalized tax rate going forward will be a key catalyst for earnings growth.

1# Volumes to show over and above industry growth

We expect HASCOL's volumes to grow by +37%YoY in CY17E as compared to +3% for industry led by +57%YoY and +48%YoY growth in MS and HSD sales. Whereas, we estimate HASCOL's total volumes to grow by +5%/+9%/+9%YoY in CY18/CY19/CY20F.

2# MS and HSD market share to reach 13% each by CY19 from 8% in CY16

Accordingly, we expect HASCOL's market share to reach 13% each for MS and HSD by CY19 on the back of a) improved demand and, b) aggressive expansion in retail outlet and storage facilities to capture smaller OMCs market share. HASCOL is currently 2nd largest OMC operating in Pakistan based on volumes sold which are expected to clock in at 2.55mn tons by the end of CY17 as compared to 14.01mn ton, 2.51mn tons and 2.08mn ton for PSO, SHEL and APL, respectively.

3# Retail outlets expansion to remain key strategic goal for the company

HASCOL as of Jun-2016 stood at 342 retail outlets across Pakistan primarily focused in Sindh and Punjab. Following the strategy of expansion to grab market share, the company plans to reach 500 retail outlets by the end of CY17. As HASCOL has remained aggressive to target CPEC routes and has been the first to expand, we believe the company to surpass 600 retail outlets by CY19F.

Recommendation

We maintain a **'BUY'** call on HASCOL with revised Dec-17 TP of PKR 389/share (down by 9% from previous PKR 430/share) offering an upside of +35% from its last close. The company is currently trading at CY17E/CY18E P/E of 20.8x/17.3x and dividend yield of 3.1%.

Contents

Investment Summary 3
- Sector performance 3
- Investment thesis 3
- CY17 earnings estimates revised down to PKR 13.8/share (down by 19%) 5
- Valuation 5
- Recommendation 5

Earnings to post 3Yr forward CAGR of +26% from CY18-20F 6
- However, despite downward earnings revision we estimate earnings to still post double digit growth over the next 3Yr 6

Superior display on volumetric growth; making it the second largest OMC of Pakistan 7
- Volumes to show over and above industry growth 7
- HASCOL has doubled its market share in a span of two years; 4% in CY14 to 8% in CY16… 8
- …and it's expected to reach 13% by CY19 8

Margin revision on the cards 9
- Annual OMC margins linked with CPI 9
- Sensitivity of MS and HSD margins on profitability and target price 9
- OMCs demand further increase in margins above the agreed inflation rate 10
- HASCOL will be prime beneficiary of any increase in MS and HSD OMC margins 10
- Sensitivity of earnings to additional increase in OMC margin 10

Right Issue for Expanding Storage Capacity and Retail Outlet 11
- HASCOL declared 20% right issue at a premium of PKR 155/share for its storage and retail outlet expansion 11
- Storage capacity to reach 331,950 Mton by CY19 from current 95,350 Mton 11
- Hascol Terminals to enhance storage capacity massively 11
- Retails outlets expansion to remain key strategic goal for the company 12
- Expansion in storage and retail outlet in Kotla Jam and Thalian lies on the CPEC route 12

Tax rate to normalize from CY18 onwards 13
- Deferred tax to dent CY17E bottom-line, however effective tax rate (ETR) is expected to normalize from CY18 onwards 13
- Selling and Admin expense to remain on the higher side 13

Outlook 14
- Summary 14
- Earnings growth 14
- Volumetric growth factor 14
- Annual margins accretion of MS and HSD linked with CPI inflation 14
- Normalized tax rate of 30% from CY18 onwards 14
- Storage facility expansion 14
- Retail outlet growth to be prime factor for earnings growth 14

Key Catalyst 15
Key Risks 15
Financial Highlights 16
Result Review; 2QCY17 17
- 2QCY17 Earnings Review; HASCOL posted earnings of PKR 3.43/share 17

Investment Summary

Sector performance

OMC sector earnings are up by +57% in 1HCY17, while HASCOL's earnings are up by +29% in 1HCY17. Despite growth in sector earnings, OMC sector performance is down by 6% in CY17TD compared to KSE-100 down by 10% over concerns of delay in OMC margin revision for MS and HSD earlier linked with CPI inflation. HASCOL's share price is down by 15% in CY17TD on account of lower than expected earnings on the back of higher effective tax rate and selling/distribution expenses, despite upbeat growth in volumes.

Investment thesis

We maintain our Over-Weight stance on HASCOL as the company is expected to benefit most from margin revision and capture additional demand emanating from CPEC projects. As a result, we estimate double digit earnings growth story to continue, posting a 3Yr forward CAGR of +26%. We base our investment case on the following:

- We expect volumes to surge massively, increasing the market share to 13%/13% for MS/HSD by CY19F as compared to 3% for each in CY14. We expect HASCOL's volumes to grow by +37%YoY in CY17E led by +57%YoY and +48%YoY growth in MS and HSD sales. Whereas, we estimate HASCOL's total volumes to grow by +5%/+9%/+9%YoY in CY18/CY19/CY20F. However, for MS we expect HASCOL to keep on capturing other OMCs margins till CY19 and post +10%/+19%/+14%YoY increase in CY18/CY19/CY20F. While, HSD sales are foreseen to rise by +5%/+5%/+9%YoY in CY18/CY19/CY20F.
- Annual margins accretion of MS and HSD linked with CPI inflation. We estimate annual margin accretion linked with CPI to augment earnings by PKR 0.3/share/PKR 2.6/share/PKR 5.2/share in CY17E/18F/19F. We have assumed CPI inflation of 5% from CY18 onwards, while weighted average margin for CY17 owing to delay is estimated at PKR 2.43/ltr for MS and HSD, respectively.
- Higher effective tax rate of 44% in CY17E is expected to shred earnings by PKR 3.18/share (from average base tax rate of 31.5% for CY17E). However, from then onwards in CY18 we estimate effective tax rate to normalize at 30%.

Other key catalysts include aggressive expansion in to retail outlets and storage facilities. Retail outlets are expected to increase to 600 by CY19F which currently stands at around 360 retail outlets, while storage facility is expected to reach 331,950 Mton by CY19F from current 95,350 Mton.

As a result, we expect HASCOL's market share to reach 11% by CY19 (13% each for MS and HSD) owing to a) improved demand and, b) aggressive expansion in retail outlets and storage facilities to capture smaller OMCs market share. HASCOL is currently the 2nd largest OMC operating in Pakistan based on the volumes. To recall, the company had managed to attain a total market share of 8% by CY16 from 4% in CY14 as a result of aggressive expansion in storage facilities and retail outlets.

Exhibit:
OMC sector has underperformed the benchmark index in the past 6M despite better earnings growth

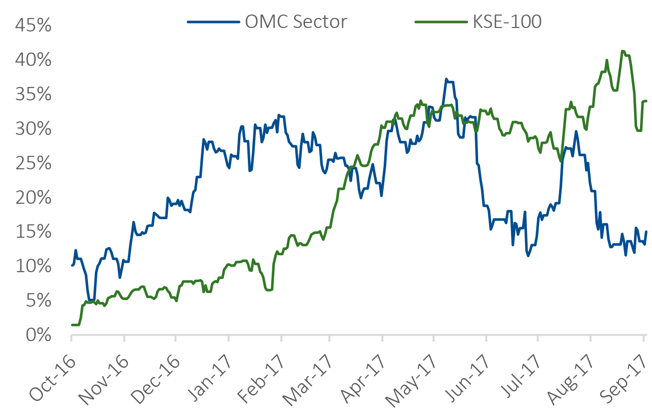
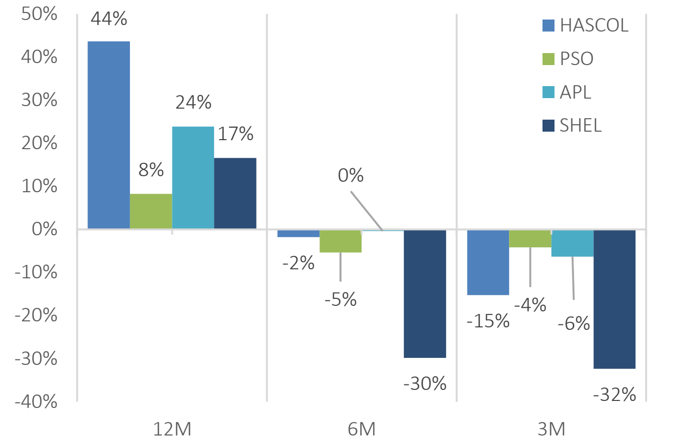


Exhibit:
Key among the sector underperformance was SHEL followed by HASCOL in last 3M



Source: IGI Research, Company Financials, Bloomberg, PSX

Exhibit:
However, on 12M basis HASCOL has outperformed; with +44% return

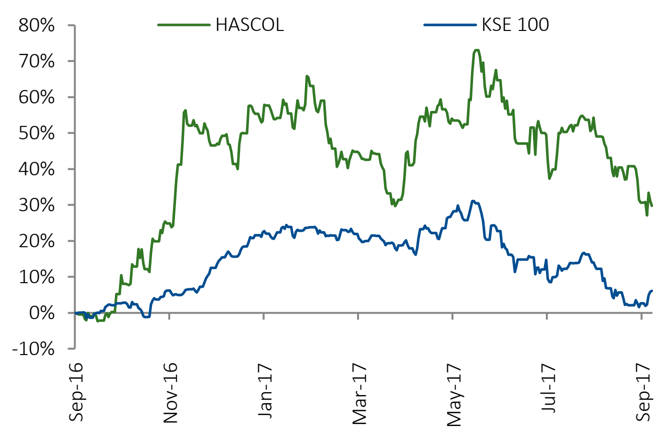
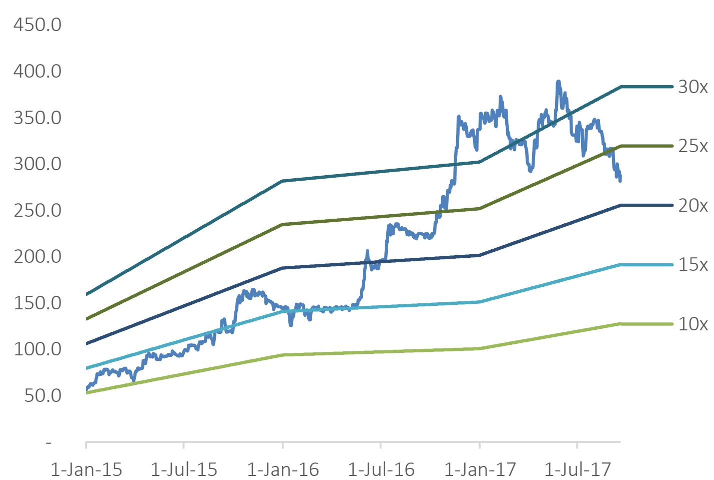


Exhibit:
The company is trading close to its 12M average PER despite improving fundamentals



Source: IGI Research, Company Financials

CY17 earnings estimates revised down to PKR 13.8/share (down by 19%)

We have revised down our earnings estimates for Hascol Petroleum Limited (HASCOL) to PKR 13.83/share / PKR 16.59/share / PKR 21.19/share (down by 19%/30%/32%) for CY17E/18F/19F.

We base our earnings revision on the back of;

- higher tax rate owing to standing deferred tax liabilities in CY17,
- Higher selling and distribution costs on the back of increased sales promotion and advertising; and
- Delays in margin increase for MS and HSD for FY18.

As a result, we have revised down our target price for HASCOL to PKR 389.4/share from previous PKR 430/share (down by 9%).

Valuation

We have used Discounted Cash Flow method (DCF) for our valuation. We have used a Risk Free Rate of 6.25%, Risk Premium of 6.50% and Beta of 1.21 to come up with a cost of equity of 14.1%.

Recommendation

We maintain a **'BUY'** call on HASCOL with revised Dec-17 TP of PKR 389/share (down by 9% from previous PKR 430/share) offering an upside of +35% from its last close. The company is currently trading at CY17E/CY18E P/E of 20.8x/17.3x and dividend yield of 3.1%.

Exhibit
Valuation Snapshot

Symbol	Market Cap		P/E (x)			Earnings Growth (%)			TP PKR/Share
	PKR bn	USD bn	CY17E	CY18F	CY19F	CY17E	CY18F	CY19F	
HASCOL	34.69	0.33	20.79	17.33	13.57	37%	20%	28%	**389.41**

Source: IGI Research

Earnings to post 3Yr forward CAGR of +26% from CY18-20F

However, despite downward earnings revision we estimate earnings to still post double digit growth over the next 3Yr

We maintain our investment thesis on the back of higher earnings growth led by superior volumetric growth in retail segment. We expect HASCOL to post 3Yr earnings CAGR of +26% from CY18-20F on the back of;

- +25% rise in total volumes led by +50%/+20%YoY increase in MS/HSD volumes,
- Annual margins accretion of MS and HSD linked with CPI inflation and,
- Normalized tax rate of 30% from CY18 onwards as all deferred tax liability is expected to be fully expensed out by the end of CY17.

Market share is expected to increase owing to aggressive expansion compared to other larger OMCs. Key catalyst for earnings growth remains excess demand emanating from CPEC which is currently the company's prime focus area for retail outlet and storage capacity expansion.

Exhibit:
Double digit earnings growth to continue till CY19

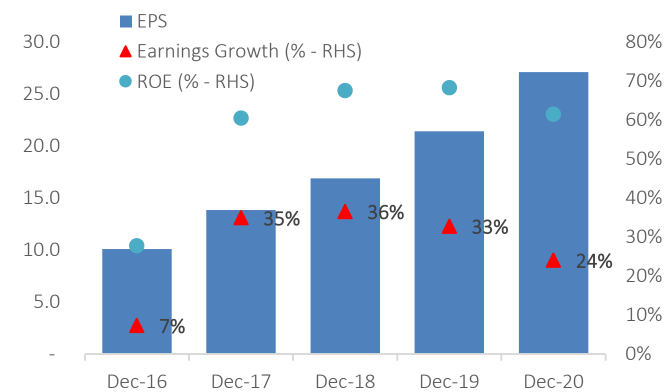
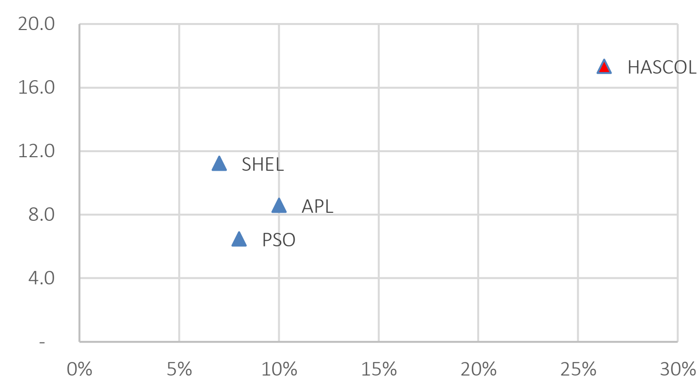


Exhibit:
Standing tall among peers: Higher earnings growth justifies higher P/E



Source: IGI Research, Company Financials (growth=3Yr CAGR)

Exhibit:
OMC Sector Highlight

Company	Market Cap (USD mn)	EPS (PKR)		P/E x		Earnings Growth (%)		Dividend Yield (%)		ROE (%)	
		FY17/CY17	FY18/CY18	FY17/CY17	FY18/CY18	FY17/CY17	FY18/CY18	FY17/CY17	FY18/CY18	FY17/CY17	FY18/CY18
PSO	1,173	68.39	69.93	6.61	6.47	81%	2%	4%	5%	19%	17%
HASCOL	331	13.83	16.59	20.79	17.33	37%	20%	3%	3%	26%	28%
APL	495	67.85	72.86	9.22	8.59	47%	7%	8%	9%	38%	37%
SHEL	418	30.06	36.47	13.63	11.24	-52%	21%	4%	5%	27%	30%

Source: IGI Research, PSX

Superior display on volumetric growth; making it the second largest OMC of Pakistan

Volumes to show over and above industry growth

We expect HASCOL's volumes to grow by +37%YoY in CY17E led by +57%YoY and +48%YoY growth in MS and HSD sales. Whereas, we estimate HASCOL's total volumes to grow by +5%/+9%/+9%YoY in CY18/CY19/CY20F. However, for MS we expect HASCOL to keep on capturing other OMCs margins till CY19 and register +10%/+19%/+14%YoY increase in CY18/CY19/CY20F. While, HSD sales are foreseen to rise by +5%/+5%/+9%YoY in CY18/CY19/CY20F. We expect above industry growth in CY20 for HASCOL owing to additional storage capacity coming online at Port Qasim, Hub, Thalian and Kotla Jam. We believe a stagnant growth in FO volumes in line with industry growth despite 112,000Mton expansion coming online in CY19 at Port Qasim (a joint venture with Vitol) on the back of shift in generation mix to coal, hydel and LNG once power projects come online. The company however, has private customers operating captive power plants on Furnace Oil (FO) but that will also shift to cheaper sources, in our view.

Exhibit:
HASCOL: MS and HSD volumes to stay ahead of industry volumes

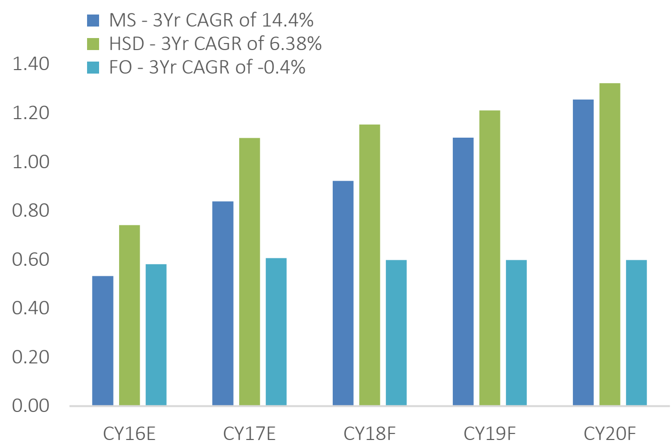
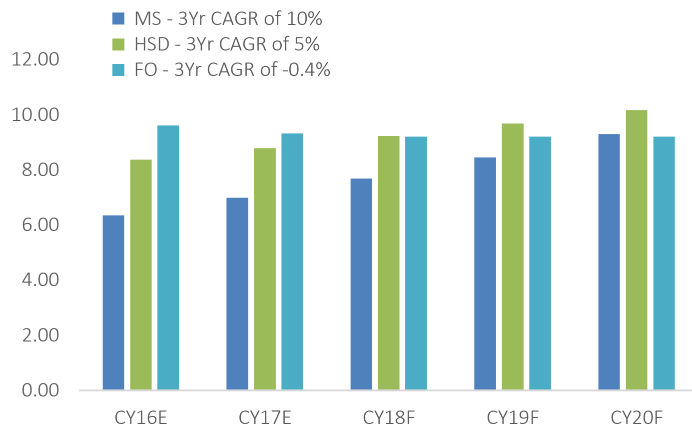


Exhibit:
Industry: MS and HSD driving total volumes



Source: IGI Research, Company Financials

HASCOL has doubled its market share in a span of two years; 4% in CY14 to 8% in CY16…

To recall, HASCOL stood at a total market share of 4% in CY14 with MS and HSD market share of 4% and 5%, respectively. Taking advantage of first mover in expansion of storage and retail outlets to capture excess demand emanating from lower domestic prices and increased passenger car sales, while market leaders such as PSO and SHEL were restricted due to cash constraints. As a result, the company managed to increase its market share from 4% in CY14 to 8% in CY16 with MS/HSD market share increasing from 4%/5% to 8%/9% by CY16.

Exhibit:
OMC Industry Market Share for MS (CY basis)

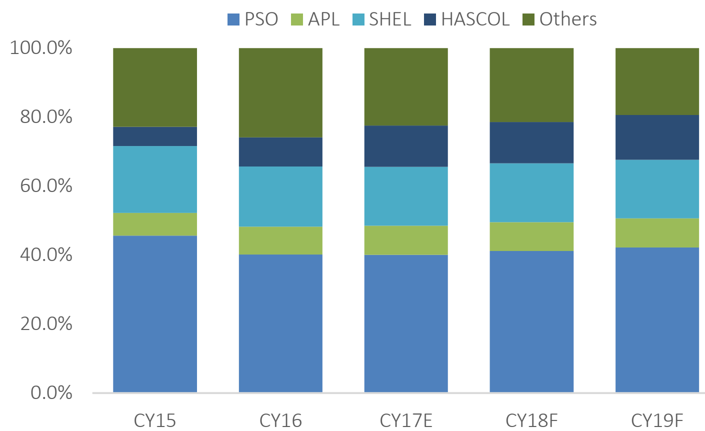
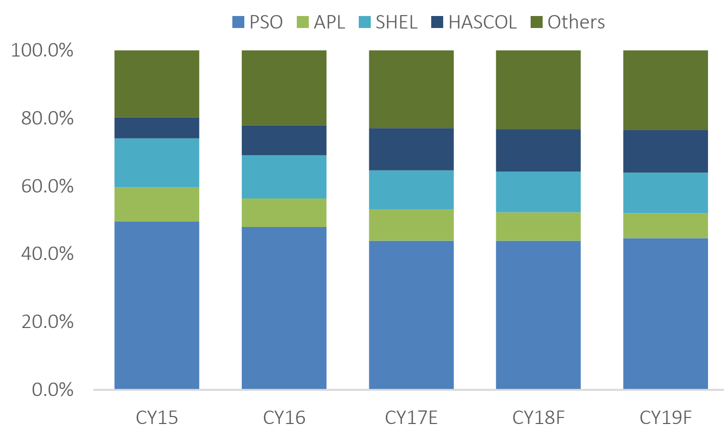


Exhibit:
OMC Industry Market Share for HSD (CY basis)



Source: IGI Research, Company Financials

…and it's expected to reach 13% by CY19

Accordingly, we expect HASCOL's market share to reach 13% each for MS and HSD by CY19 on the back of a) improved demand and, b) aggressive expansion in retail outlet and storage to capture smaller OMCs market share. HASCOL is currently the 2nd largest OMC operating in Pakistan based on volumes sold which are expected to clock in at 2.55mn tons by end of CY17 as compared to 14.01mn ton, 2.51mn tons and 2.08mn ton for PSO, SHEL and APL, respectively.

Exhibit:
HASCOL MS market share to reach 13% by CY19

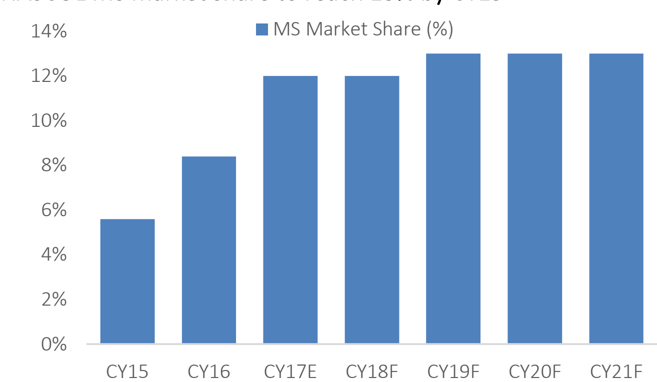
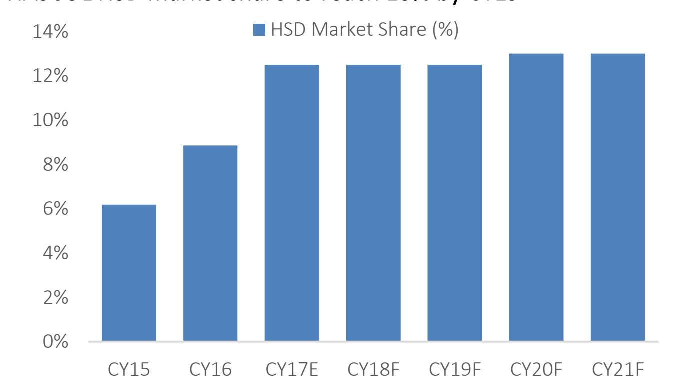


Exhibit:
HASCOL HSD market share to reach 13% by CY19



Source: IGI Research, Company Financials

Margin revision on the cards

Annual OMC margins linked with CPI

In May-16, the Economic Coordination Committee (ECC) on recommendation of Ministry of Petroleum and Natural Resources (MPNR) approved annual increase of 0.06/ltr in OMCs margins for MS and HSD, along with annual revision thereon linked with CPI. We have assumed base case CPI inflation of 5% during FY19F-FY21F (CPI inflation of 4.16% for FY17), augmenting HASCOL's weighted average margins by 5% in CY18 and CY19 for MS and HSD, respectively. Considering that there has been a delay of 3 months in issuance of notification of margin increase for FY18, we have assumed weighted average margin of PKR 2.43/ltr for MS and HSD each as it is likely to be approved in the next ECC meeting to be held by mid of Sep-17. As a result, we expect earnings to catalyze by PKR 0.3/share/PKR 2.6/share/PKR 5.2/share in CY17E/18F/19F.

Exhibit:
Weighted average margin for MS & HSD

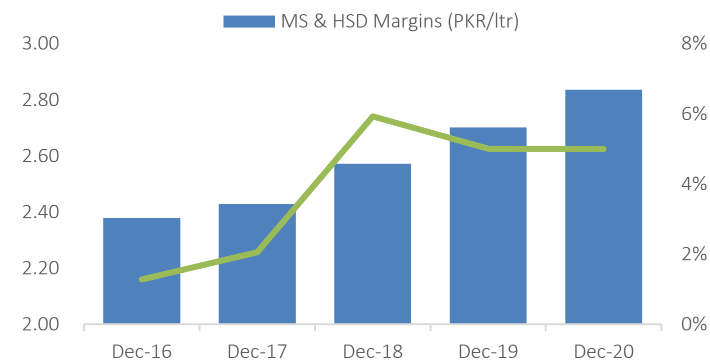
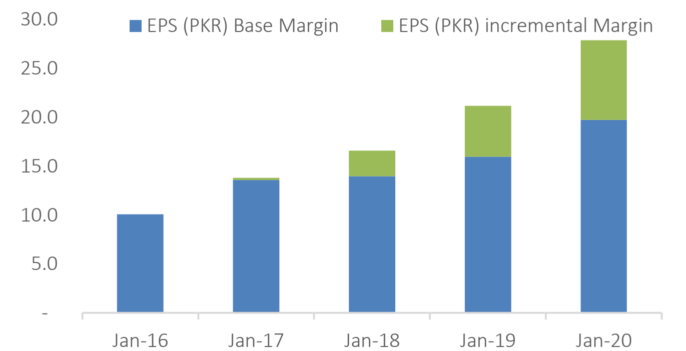


Exhibit:
Contribution to revenue of increased margins



Source: IGI Research, OGRA, Company Financials

Sensitivity of MS and HSD margins on profitability and target price

According to latest prices notified by OGRA and PSO for Sep-17, the OMC margin for MS and HSD are currently standing at the previous rate of PKR 2.41/ltr each, which were to be increased linked with CPI from Jul-17 onwards. The price increase has been delayed for nearly 3 months now and the matter to increase the margins was deferred in the last ECC meeting held at the end of Aug-17, which in our view is likely done on purpose to provide relief of lower prices to consumers. However, we believe revised OMC margins will be approved in the next ECC meeting and will be effective from Oct-17, which is our base case assumption. Below is the table of earnings impact of further delay in notification of increase in OMC margins.

Exhibit:

Sensitivity of earnings in respect of further delays (MS &HSD)

PKR/share	OMC Margin (CY)	CY17E	% Change
Base Case *	2.43	13.83	-
Bear Case 1 (Nov-17)	2.43	13.78	-0.37%
Bear Case 2 (Dec-17)	2.42	13.71	-0.86%
Bear Case 3 (Jan-17)	2.41	13.58	-1.83%

Source: IGI Research

OMCs demand further increase in margins above the agreed inflation rate

According news report the OMCs are demanding a PKR 0.4/ltr further increase in margins owing to delays in decision making.

> News report extract:
> ***Profit margins of oil companies, dealers likely to go up:*** *"The maiden meeting of the reconstituted Economic Coordination Committee (ECC) of the cabinet is expected this week to consider increasing profit margins of oil marketing companies (OMC) and dealers through prices of petroleum product … Now the dealers and OMCs are also demanding a 0.4 paisa per litre increase on account of delay in the decision-making, he said."*
> *https://www.dawn.com/news/1351549*

HASCOL will be prime beneficiary of any increase in MS and HSD OMC margins

It is pertinent to mention here that HASCOL will be the prime beneficiary of any increase in MS and HSD margins as both the products cumulatively contribute nearly 63% of the total sales of HASCOL leading to greater impact on earnings compared to its peers.

Sensitivity of earnings to additional increase in OMC margin

OMC demand an additional PKR 0.4/ltr increase in the OMC margins for MS and HSD over and above the agreed PI inflation rate. Any additional increase would have 3%-10% increase in earnings in CY17E and 4%-17% increase in CY18F earnings depending on the amount of additional margin increase approved ranging between PKR 0.1-0.4/ltr. Below is a sensitivity table of increase in earnings based on margin increase between the ranges of PKR 0.1/ltr and PKR 0.4/ltr.

Exhibit:

OMC margin sensitivity (MS &HSD)

PKR/share	OMC Margin (FY)	Growth	OMC Margin (CY17)	OMC Margin (CY18)
Base Case *	2.51	0.0%	2.46	2.57
Best Case 1 (+0.1)	2.61	4.0%	2.56	2.68
Best Case 2 (+0.2)	2.71	8.0%	2.66	2.78
Best Case 3 (+0.3) *	2.81	12.0%	2.76	2.88
Best Case 3 (+0.4)	2.91	15.9%	2.86	2.98

HASCOL Earnings Sensitivity

	CY17E	% Change	CY18F	% Change
Base Case	13.83	-	16.59	-
Best Case 1 (+0.1)	14.03	1.42%	18.14	9.34%
Best Case 2 (+0.2)	14.25	3.04%	19.69	18.69%
Best Case 3 (+0.3)	14.48	4.67%	21.25	28.04%
Best Case 3 (+0.4)	14.70	6.30%	22.80	37.39%

Source: IGI Research

* Best Case earnings are estimated assuming the margins are revised from Oct-17 and base case margins are after the agreed increase based on FY17 CPI inflation that is 4.16%.

Right Issue for Expanding Storage Capacity and Retail Outlet

HASCOL declared 20% right issue at a premium of PKR 155/share for its storage and retail outlet expansion

According to notice issued by HASCOL on Pakistan Stock Exchange (PSX), the company has announced a right share issue of 20% (20 shares for every 100 shares held) at a premium of PKR 155/share. As a result, the company is expected to raise PKR 3.98bn through proceeds of right share issue through an additional 24.14mn shares taking total outstanding number of shares to 144.82mn. The management outlined the following plan for utilization of proceeds from right issue:

Exhibit:

Management Plan for Utilization of Proceeds

Quantum of Issue	The issue size is 20% of existing capital (24,135,840 ordinary shares) i.e. 20 shares for every 100 shares held.
Issue Price	The Right shares will be offered at an issue price of Rs. 165/- per share, including premium of Rs.155 per share.
Purpose of Rights Issue	The purpose of the Rights Issue is to fund the upcoming projects including development of storage facilities, retail outlets and lube oil and grease blending plant.
Benefits to the Company	The funds received from the Rights Issue will be used towards the completion of the projects in expansion of the Company, which will increase breakup value of the Company and will also improve the debt equity ratio. The funds will enable the Company to pursue its growth strategy resulting in increased revenues and profitability
Risk factors associated with the Rights Issue	There are no significant risk factors associated with the Rights Issue.

Source: PSX, IGI Research

Storage capacity to reach 331,950 Mton by CY19 from current 95,350 Mton

HASCOL's current storage capacity stands at 95,350 Mton with MS and HSD storage at 40,150 Mton and 55,200Mton, respectively compared to 16,900 Mton at the end of CY15. Company's terminal capacity currently stands at 89,600 Mton. The company plans to increase its storage capacity to 331,950 Mton by CY19 with major expansion in HSD storage. To note, Mehmood Kot extension was completed during 1HCY17.

Hascol Terminals to enhance storage capacity massively

HSD and MS storage capacity is expected to reach 150,800 Mton and 69,150 Mton from current 55,200 Mton and 41,150 Mton, respectively. Major capacity increase is estimated to come from its subsidiary Hascol Terminals at Port Qasim adding nearly 69,600 Mton and 25,000 Mton of HSD and MS capacity by the end of CY17. While for FO, capacity expansion of 150,800 Mton will come online by end of CY18.

Exhibit:
Storage capacity to reach 331,950 Mton by CY19

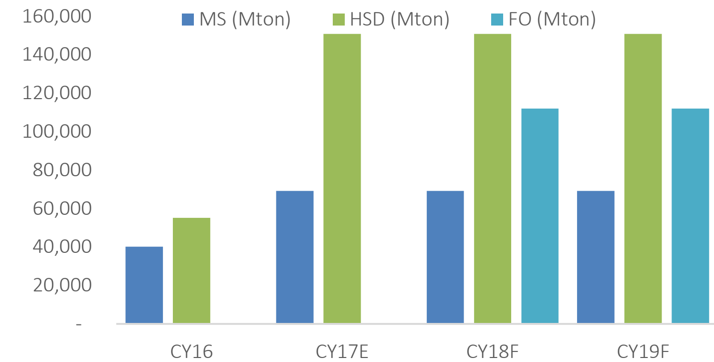
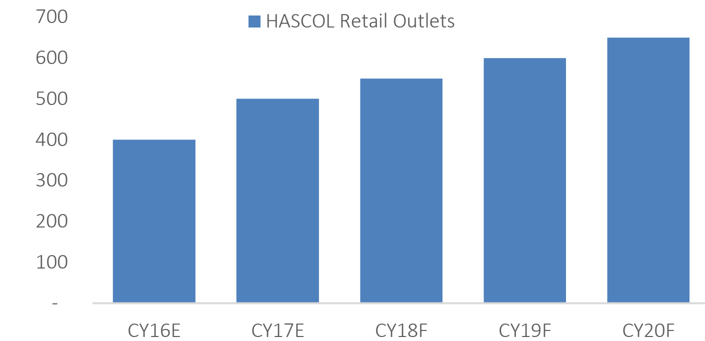


Exhibit:
Retail outlet expansion to remain robust



Source: IGI Research, Company Financials

Retails outlets expansion to remain key strategic goal for the company

HASCOL as of Jun-16 stood at 342 retail outlets across Pakistan primarily situated in Sindh and Punjab. Following the strategy of expansion to grab market share, the company plans to reach 500 retail outlets by the end of CY17. As HASCOL has remained aggressive to target CPEC routes and be the first to expand, we believe the company to cross 600 retail outlets by CY19. According to the company's recent interim financial report the company currently stands as the second largest OMC operating in Pakistan.

Expansion in storage and retail outlet in Kotla Jam and Thalian lies on the CPEC route

HASCOL's expansion in to retail outlet and storage facility in Kotla Jam, Hub and Thalian lie on the CPEC route. HASCOL is targeting the CPEC route to benefit from the rising commercial transport through CPEC routes leading to higher volumes. Moreover, Kotla Jam remains an under developed area in terms of OMC where only PSO currently has its retail presence. With improved demand through CPEC, this area should provide further volume uptick for HASCOL once CPEC projects gains traction.

Exhibit:
Kotla Jam and Thalian Lies on CPEC route

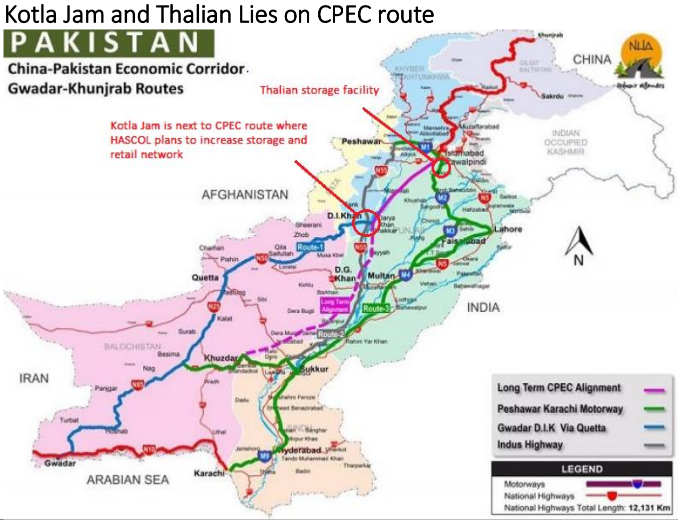
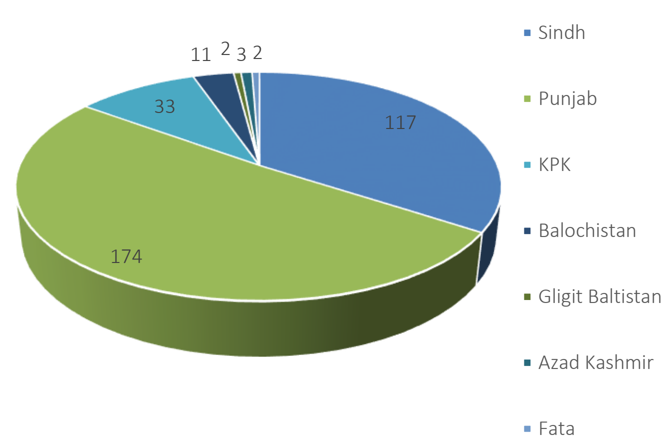


Exhibit:
Province Wise Retail Outlets as of FY16



Source: IGI Research, National Highway Authority, OCAC Oil Report 2015-16, Company Financials

Tax rate to normalize from CY18 onwards

Deferred tax to dent CY17E bottom-line, however effective tax rate (ETR) is expected to normalize from CY18 onwards

HASCOL reported effective tax rate of 44% in CY16 compared to 5% and 26% reported in CY15 and CY14, respectively. The rise in effective tax rate was due to deferred tax liability arising from a change to corporate tax rate from turnover tax rate. We believe higher tax rate to continue during 2HCY17 and normalize from CY18 onwards. Accordingly based on our estimates, higher effective tax rate of 44% in CY17E is expected to shred earnings by PKR 3.18/share (from average base tax rate of 31.5% for CY17E).

Exhibit:
ETR high owing to deferred tax (Quarterly - %)

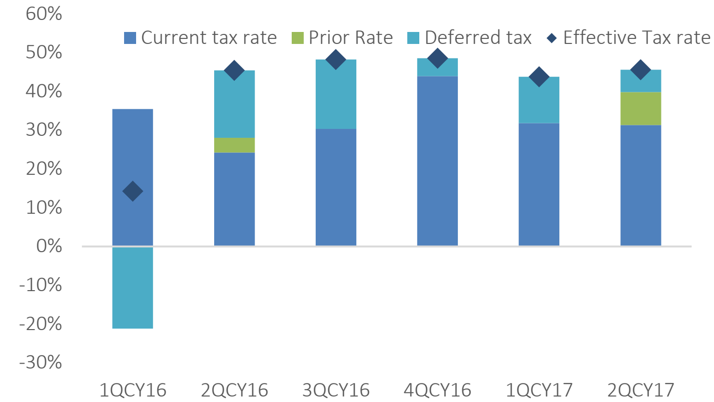
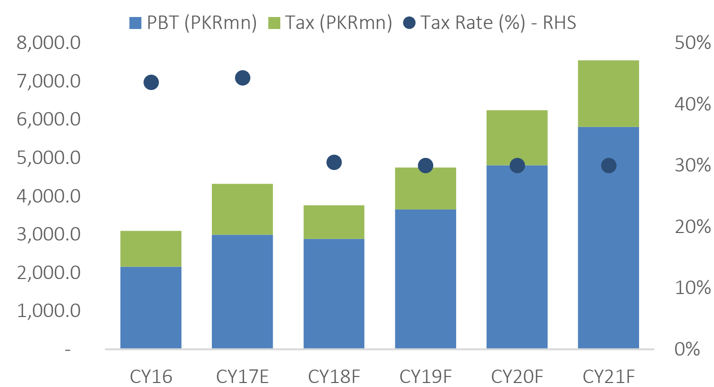


Exhibit:
Effective tax rate to normalize going forward



Source: IGI Research, Company Financials

Selling and Admin expense to remain on the higher side

The company reported a +51%YoY and +52%YoY jump in selling and distribution cost during 1QCY17 and 2QCY17, respectively. This is likely due to higher sales promotion and salaries expense for to aggressive marketing and expansion strategy. We expect selling/distribution and administrative expenses to rise by +26%YoY in CY17E compared to +61%YoY rise in CY16. From CY17 onwards we expect operating expenses to rise by 10%-12%YoY till CY21.

Exhibit:
Quarterly Selling & admin expense (PKRmn)

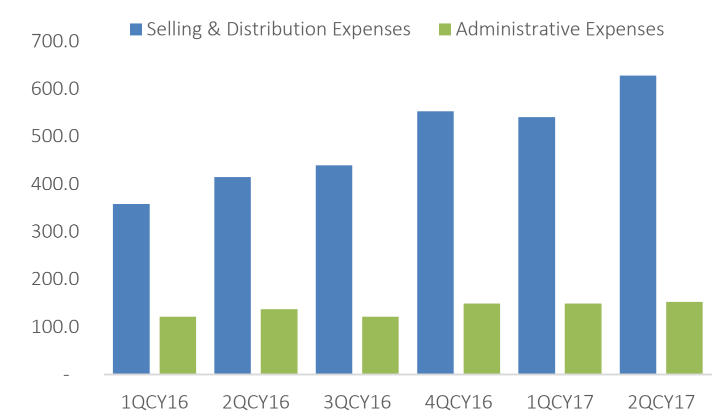
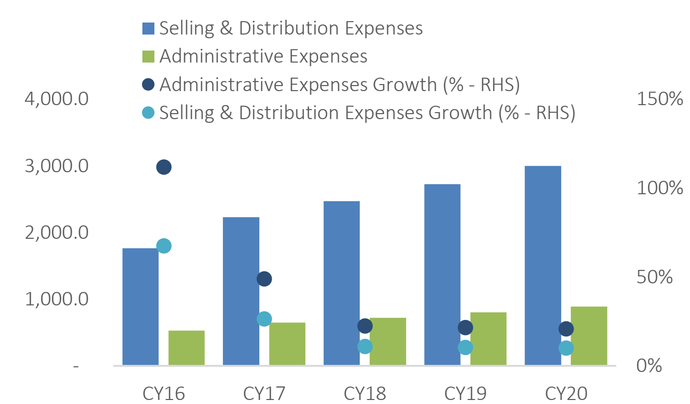


Exhibit:
Operating expenses to remain on the higher side (PKRmn)



Source: IGI Research, Company Financials

Outlook

Summary

We expect higher growth in HASCOL's volumes to drive earnings going forward based on aggressive expansion in storage facilities and retail outlets.

Earnings growth

We expect HASCOL to post 3Yr earnings CAGR of +26% from CY18-20F on the back of a) +25% rise in total volumes led by +50%/+20%YoY increase in MS/HSD volumes, b) annual margins accretion of MS and HSD linked with CPI inflation; and c) normalized tax rate of 30% from CY18 onwards as substantial deferred tax liability is expected to be utilized by the end of CY17.

Volumetric growth factor

As a result of this, we expect volumes to surge massively, increasing the market share to 13%/13% for MS/HSD by CY19F as compared to 3% for each in CY14. We expect HASCOL's volumes to grow by +37%YoY in CY17E led by +57%YoY and +48%YoY growth in MS and HSD sales. Whereas, we estimate HASCOL's total volumes to grow by +5%/+9%/+9%YoY in CY18F/CY19F/CY20F. However, for MS we expect HASCOL to keep on capturing other OMCs margins till CY19 and post +10%/+19%/+14%YoY increase in CY18F/CY19F/CY20F. While, HSD sales are foreseen to rise by +5%/+5%/+9%YoY in CY18/CY19/CY20F. We believe a stagnant growth in FO volumes in line with industry growth despite 112,000Mton expansion coming online in CY19 at Port Qasim.

Annual margins accretion of MS and HSD linked with CPI inflation

We estimate annual margin accretion linked with CPI to augment earnings by PKR 0.3/share/PKR 2.6/share/PKR 5.2/share in CY17E/18F/19F. We have assumed CPI inflation of 5% from CY18 onwards, while weighted average margin for CY17 owing to delay is estimated at PKR 2.43/ltr for MS and HSD, respectively.

Normalized tax rate of 30% from CY18 onwards

Higher effective tax rate of 44% in CY17E is expected to shred earnings by PKR 3.18/share (from average base tax rate of 31.5% for CY17E). However, we anticipate effective tax rate to normalize at 30% from CY18 onwards.

Storage facility expansion

HASCOL's current storage capacity stands at 95,350 Mton with MS and HSD storage at 40,150 Mton and 55,200 Mton respectively compared to 16,900 Mton at the end of CY15. The company plans to increase its storage capacity to 331,950 Mton by CY19 with major expansion in HSD storage. HSD and MS storage capacity is expected to reach 150,800 Mton and 69,150 Mton from current 55,200 Mton and 41,150 Mton, respectively.

Retail outlet growth to be prime factor for earnings growth

HASCOL currently stands at 460 retail outlets all over Pakistan. As part of aggressive expansion strategy, the company plans to increase its retail outlets to 500 by the end of CY17 which as of Jun-16 stood at 342. We expect the company to increase its retail network to 600 retail outlets by 2019. Moreover to highlight, the expansion plan of retail network is majorly focused to target the demand emanating from CPEC.

Key Catalyst

- Supply agreement with Vitol to mitigate hefty inventory losses in times of steep drop in oil prices
- Actual demand emanating from CPEC for MS and HSD to materialize more than expectation providing further growth in volumes and consequently earnings
- Improvement in macro-economic environment in Pakistan

Key Risks

- One of the major risk remains volatility in oil prices and as HASCOL increases it storage capacity it will be vulnerable to hefty inventory losses.
- Further delays in margin revision will lead to further loss in profitability
- PKR depreciation will lead to foreign exchange losses and higher costs leading to increase in domestic prices

Financial Highlights

Hascol Petroleum Limited (HASCOL)

Current Price (PKR): **288** Target Price (PKR): **389** Upside Recommendation: **BUY**

Period end (Dec) - PKRbn	CY15A	CY16A	CY17E	CY18F	CY19F	CY20F
Income Statement Items						
Net Sales	76.8	99.5	136.8	153.7	174.6	198.3
Gross Profit	2.8	4.7	6.2	7.0	8.1	9.5
Selling & Distr. Expense	1.1	1.8	2.2	2.7	3.0	3.3
Admin Expense	0.4	0.5	0.6	0.7	0.8	0.9
Other Income	0.2	0.2	0.2	0.3	0.3	0.3
EBIT	1.6	2.6	3.5	3.9	4.6	5.6
Finance Costs	0.3	0.4	0.5	0.9	0.9	0.8
Pre-tax Profits	1.2	2.2	3.0	2.9	3.7	4.8
Post- Tax Profits	1.1	1.2	1.7	2.0	2.6	3.4
Balance Sheet Items						
PPE	6.3	8.7	10.5	12.1	13.7	14.3
LT Invst.	2.0	2.0	2.0	2.0	2.0	2.0
Non Current Assets	8.7	10.9	12.8	14.5	16.1	16.9
Inventory	8.5	16.5	22.2	24.8	27.9	31.7
Trade debts	4.3	7.9	10.9	12.6	14.6	16.5
Total Assets	26.6	44.6	54.7	58.7	65.5	72.9
Payables	17.4	29.8	39.3	42.3	48.0	54.4
Current Liab.	20.2	35.0	45.1	48.8	55.0	61.4
LT Debt	0.2	2.3	2.2	1.5	0.9	0.3
Non Current Liab.	0.6	3.5	2.9	2.3	1.7	1.3
Total Liab.	20.8	38.5	47.9	51.0	56.7	62.7
Share Capital	1.2	1.2	1.2	1.2	1.2	1.2
Total Equity	5.8	6.1	6.8	7.6	8.8	10.2
Cash Flow Items (PKRbn)						
Operating CF	4.7	1.5	2.7	1.9	4.3	4.9
Investing CF	(6.3)	(2.0)	(2.9)	(2.4)	(2.4)	(1.7)
Financing CF	1.7	4.1	(1.0)	(1.8)	(2.0)	(2.5)
Cash	4.1	7.8	6.6	4.3	4.1	4.8
Per Share						
EPS	9.4	10.1	13.8	16.6	21.2	27.9
DPS	5.0	7.0	8.0	9.0	12.0	16.0
BV	47.9	50.6	56.0	63.3	72.6	84.9
Cash	33.7	64.8	54.6	35.6	34.1	39.7

Period end (Dec) - PKRbn	CY15A	CY16A	CY17E	CY18F	CY19F	CY20F
Valuation						
P/E (x)	30.6	28.5	20.8	17.3	13.6	10.3
P/EBITDA (x)	1.9	1.1	0.9	0.8	0.6	0.5
D/Y (%)	1.7	2.4	2.8	3.1	4.2	5.6
P/B (x)	6.0	5.7	5.1	4.5	4.0	3.4
ROE (%)	25.51	20.45	25.95	27.81	31.17	35.39
ROA (%)	5.37	3.41	3.36	3.53	4.12	4.86
Margins						
Gross Margins (%)	3.7	4.7	4.5	4.6	4.7	4.8
EBIT Margin (%)	2.1	2.6	2.6	2.5	2.6	2.8
Net Profit Margins (%)	1.5	1.2	1.2	1.3	1.5	1.7
Financial Gearing						
Total Debt / Equity (%)	3.0	37.8	32.4	19.7	10.3	3.2
Interest Coverage	4.7	6.1	7.0	4.2	5.1	7.4
Efficiency Ratios						
Current Ratio	0.9	1.0	0.9	0.9	0.9	0.9
Quick Ratio	0.5	0.5	0.4	0.4	0.4	0.4
Cash Cycle						
Cash Cycle	(22.7)	(45.6)	(36.0)	(35.0)	(35.0)	(35.0)
Inventory Days	23.2	46.7	46.0	46.0	46.0	46.0
Receivable Days	17.1	22.3	23.0	24.0	24.0	24.0
Payable Days	62.9	114.6	105.0	105.0	105.0	105.0
Volumes (mn'tons)						
Total Sales	1.27	1.86	2.55	2.68	2.91	3.18
MS	0.30	0.53	0.84	0.92	1.10	1.26
HSD	0.47	0.74	1.10	1.15	1.21	1.32
FO	0.50	0.58	0.61	0.60	0.60	0.60
Market Share (%)						
Total	6%	7%	10%	10%	10%	11%
MS	6%	8%	12%	12%	13%	14%
HSD	6%	9%	13%	13%	13%	13%
FO	6%	6%	7%	7%	7%	7%

Source: IGI Research, Company Financials

Updated as of : 9/19/2017

Exhibit: HASCOL volumes (000' MTon)

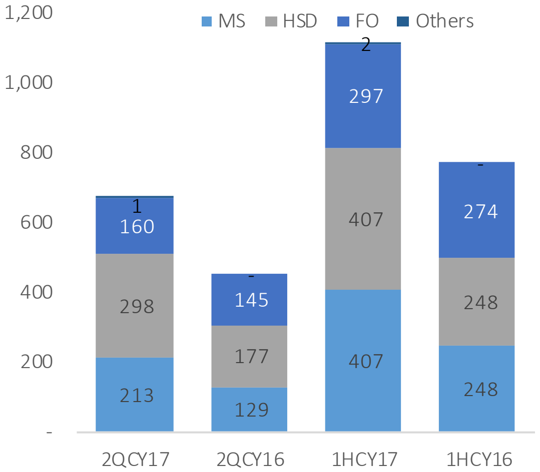
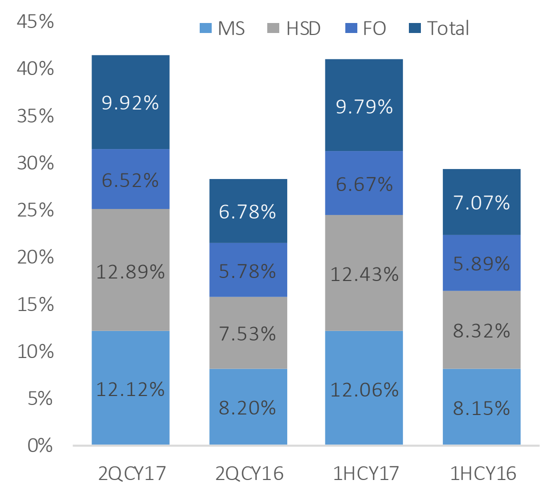


Exhibit: HASCOL - MS, HSD, FO market share



Source: Company Financials, IGI Research

Result Review; 2QCY17

2QCY17 Earnings Review; HASCOL posted earnings of PKR 3.43/share

HASCOL announced financial results for 2QCY17 with earnings clocking in at PKR 414Mn (EPS PKR 3.43) up by +1%YoY as compared to PKR 410mn (EPS PKR 3.40) in the same period last year. We attribute this meagre growth in earnings to a) higher effective tax rate of 45.6%, b) +52%/+11%YoY increase in selling & marketing/administrative expense, c) gross margins declined to 3.8% in 2QCY17 compared to 6.1% in the same period last year likely owing to higher discounts offered and inventory losses incurred during the period and, d) +37%YoY increase in finance costs. However, total sales increased by +49%YoY led by +64%/+68%/+10%YoY increase in MS/HSD/FO sales.

On quarterly basis, earnings increased by +10%QoQ, taking 1HCY17 earnings to PKR 791mn (EPS PKR 6.55) up by +29%YoY. The company announced cash dividend of PKR 3.5/share in 1HCY16 as compared to PKR 1.5/share in the same period last year.

Exhibit:

Financial Highlights

PKRmn	2QCY17	2QCY16	YoY	QoQ	1HCY17	1HCY16	YoY
Net Sales	42,848	23,015	86%	23%	77,743	43,367	79%
Gross Profit	1,622	1,407	15%	14%	3,050	2,170	41%
S&D Exp	628	414	52%	16%	1,168	772	51%
Admin Exp	152	137	11%	3%	301	258	17%
EBIT	908	893	2%	13%	1,715	1,229	39%
Finance Cost	148	108	37%	30%	262	211	24%
Profit Before Taxation	760	750	1%	14%	1,430	986	45%
Taxation	347	340	2%	18%	639	374	71%
Profit After Taxation	414	410	1%	10%	791	612	29%
EPS (PKR)	3.43	3.40			6.55	5.07	
DPS (PKR)	3.50	3.50			3.50	3.50	

Source: IGI Research, Company Financials *Shares mn: 120.68 mn*

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Recommendation	Rating System
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Hold	If target price on aforementioned security(ies) is in between -10% and 10%, from its last closing price(s)
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Time Horizon: Dec - 2017

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DCF (Discounted Cash Flow)

Risk: Investment in securities are subject to economic risk, market risk, interest rate risks, currency risks, credit risks, political and geopolitical risks. The performance of company(ies) covered herein mightunfavorably be affected by multiple factors including, business, economic, and political conditions. Hence, there is no assurance or guarantee that estimates, recommendation, opinion, etc. given about the security(ies)/company(ies) in the report will be achieved.

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IGI Finex Securities Limited
Research Analyst(s)
Research Identity Number: BRP009

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Contact Details

Research Team

Saad Khan	Head of Research	Tel: (+92-21) 111-234-234 Ext: 810	saad.khan@igi.com.pk
Abdullah Farhan	Senior Analyst	Tel: (+92-21) 111-234-234 Ext: 912	abdullah.farhan@igi.com.pk
Syed Daniyal Adil	Research Analyst	Tel: (+92-21) 111-234-234 Ext: 973	daniyal.adil@igi.com.pk
Suleman Ashraf	Research Analyst	Tel: (+92-21) 111-234-234 Ext: 957	suleman.ashraf@igi.com.pk
Muhammad Saad	Research Analyst	Tel: (+92-21) 111-234-234 Ext: 973	muhammad.saad@igi.com.pk
Tanweer Kabeer	Research/Fund Select	Tel: (+92-21) 111-234-234 Ext: 966	tanweer.kabeer@igi.com.pk
Umesh Solanki	Database Manager	Tel: (+92-21) 111-234-234 Ext: 974	umesh.solanki@igi.com.pk

Equity Sales

Faisal Jawed Khan	Head of Equities	Tel: (+92-21) 35301779	faisal.jawed@igi.com.pk
Zaeem Haider Khan	Regional Head (North)	Tel: (+92-42) 35777863-70	zaeem.haider@igi.com.pk
Muhammad Naveed	Regional Manager (Islamabad & Upper North)	Tel: (+92-51) 2604861-62	muhammad.naveed@igi.com.pk
Ejaz Rana	Regional Manager (Faisalabad)	Tel: (+92-41) 2540843-45	ejaz.rana@igi.com.pk
Asif Saleem	Branch Manager (RY Khan)	Tel: (+92-68) 5871652-56	asif.saleem@igi.com.pk
Mehtab Ali	Branch Manager (Multan)	Tel: (+92-61) 4512003	mahtab.ali@igi.com.pk
Zeeshan Kayani	Branch Manager (Abbottabad)	Tel: (+92-992) 408243-44	zeeshan.kayani@igi.com.pk
Ihsan Mohammad	Branch Manager (Peshawar)	Tel: (92-91) 5253035	ihsan.mohammad@igi.com.pk

IGI Finex Securities Limited
Trading Rights Entitlement Certificate (TREC) Holder of
Pakistan Stock Exchange Limited |
Corporate member of Pakistan Mercantile Exchange Limited

Head Office
Suite No 701-713, 7th Floor, The Forum, G-20,
Khayaban-e-Jami Block-09, Clifton, Karachi-75600
UAN: (+92-21) 111-444-001 | (+92-21) 111-234-234
Fax: (+92-21) 35309169, 35301780
Website: www.igisecurities.com.pk

Stock Exchange Office
Room # 719, 7th Floor, PSX Building, Stock Exchange Road, Karachi.
Tel: (+92-21) 32429613-4, 32462651-2 , Fax: (+92-21) 32429607

Lahore Office 5-F.C.C. Ground Floor, Syed Maratib Ali Road, Gulberg II, Lahore Tel: (+92-42) 35777863-70, 35876075-76 Fax: (+92-42) 35763542	**Islamabad Office** Mezzanine Floor, Office 5, 6 & 7, Kashmir Plaza, Block- B, Jinnah Avenue, Blue Area, Islamabad Tel: (+92-51) 2604861-2, 2604864, 2273439 Fax: (+92-51) 2273861
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