

September 10, 2009

**Pakistan Market****Refineries: Improvement in GRM's/'Buy' NRL****MORNING BRIEFING**

KSE100 Index: Closing 9084.98 ↑ (+263.42)

Net refining margins (Gross Refinery Margins GRMs-processing cost) have turned positive to US\$1 per barrel thus far in 1QFY09 versus negative US\$4 per barrel in 4QFY09. Major improvement in margins have been witnessed in diesel (HSD) and furnace oil (FO) as average spread on HSD increased to US\$9 per barrel compared to US\$5 per barrel in the preceding quarter (4QFY09). Likewise spread on FO (a loss making product for the refineries) reduced to negative US\$10 per barrel versus US\$14 per barrel in 4QFY09.

We expect NRL would be the major beneficiary as it has the highest share of HSD in its production profile. Our preliminary 1QFY10 earnings projection for NRL is Rs12-14 per share followed by ATRL (Rs4-5 per share) and PRL (loss of Rs7-9 per share). Our preferred stock in the refinery sector is NRL due to its low risk in oil price and stable lube earnings. Trading at FY10 and FY11 PE of 4.8x and 4.4x with respective dividend yield of 12.1% and 14.7%, we maintain 'Buy' stance at current levels.

**Better fuel margins expected in 1QFY10**

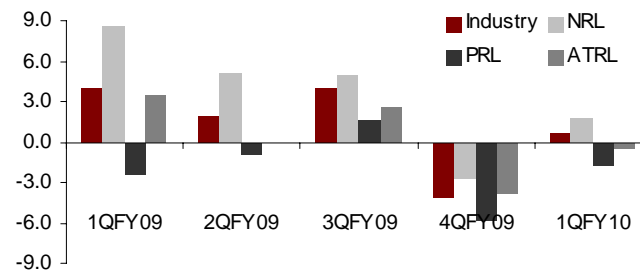
With crude oil prices remained flat QoQ, international oil market saw product prices adjusted upwards, thus improving spreads in 1QFY10 (spread=product prices less crude oil price). As per our calculation, average spread on FO so far in Jul-Sep 2009 has improved to negative US\$10/bbl v/s average spread of negative US\$14/bbl in 4QFY09. As a result, weighted average margin (GRM) on FO has reduced to negative US\$3/bbl during Jul-Sep 2009 versus negative US\$5/bbl in 4QFY09. On the other hand, margin on diesel is likely to improve to US\$3/bbl versus US\$2/bbl in 4QFY09.

**NRL: positive margins so far**

As per our estimates, NRL's average net refining margin is hovering around US\$2 per barrel in 1QFY10 versus negative US\$2.8 per barrel estimated in 4QFY09. Hence, we expect NRL to post earnings of Rs12-14/share in 1QFY10 including 9-10/share earnings contribution from lube business.

**Margins of PRL & ATRL to remain in red**

We believe fuel margins of Pakistan Refinery (PRL) and ATRL to remain in the red zone. We expect net refining margin of PRL would be ~ negative US\$2 per barrel versus negative US\$5.5 per barrel in preceding quarter while margin of ATRL is likely to be negative US\$0.5 per barrel compared to negative US\$3.8 per barrel in 4QFY09. We expect PRL to post losses some where around Rs7-9 per share in 1QFY10 while ATRL's EPS would be Rs4-5, thanks to stable earnings on bank deposits.

**Graph: Net refining margin (US\$/bbl)**

Source: OGRA &amp; JS Research

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**Also in focus****12month T-Bill yield rises to 12.48%**

In yesterday's T-bill auction, participation of Rs92bn was witnessed as against a target of Rs50bn while State Bank of Pakistan accepted Rs51.25bn. Cut off yields on the 12-month paper rose by 4bps to 12.482% while 6-month and 3-month T-bill yields came in at 12.778bps (up 23bps) and 12.517% (up 14bps).

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