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Pakistan Market**PSO: Earnings revised up 14-3% / 'Buy' maintained**

KSE100 Index: Closing 9867.09 ↑ (+97.41)

MORNING BRIEFING

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Pakistan State Oil (PSO) announced higher than expected earnings of Rs29.64 per share in 1HFY10 largely owing to interest income booked from the power generation companies. Upbeat furnace oil sales and inventory gains kept core earnings strong which had been severely hampered by inventory and exchange losses in the corresponding period last year (loss per share of Rs58.6 in 1HFY09). Moreover, the company failed to declare a widely anticipated cash dividend due to liquidity constraints emanating from the inter-corporate debt. On the back of the recent result announcement, we upgrade our earnings estimates by 14%-3% for FY10E & FY11F, respectively.

Trading at a FY10E and FY11F PE of 5.8x and 5.0x, respectively, we maintain our 'Buy' stance on the scrip.

FO sales – revenue propeller

PSO continued its strong core performance on the back of substantial growth of 27% in FO sales mainly due to rising demand from the power generation sector. Further, Motor Gasoline and Jet Fuel sales remained strong during the period with decent growths of 28% and 5%, respectively. However, HSD sales were down 5%, as local refineries opted to supply diesel fuel to other OMCs owing to concerns over prompt payments. On the lubes front, PSO managed to sell 15k tons – a growth of 25%YoY. Resultantly, the company's market share in the Black oil business increased to 89% from 87% earlier, while its overall market share stood at 70%. Hence, PSO managed to post a decent growth of 5% in net sales to Rs350bn despite significantly lower product prices. Gross profit arrived at Rs13.5bn in 1HFY10 as against a gross loss of Rs7.7bn in 1HFY09.

Inventory gains – the fairytale continues

In sharp contrast to 1HFY09 where PSO had booked inventory losses of Rs20.2bn, the company recorded inventory gains of Rs1.7bn as oil prices moved across a band of US\$62/barrel to US\$80/barel. Excluding inventory gains, PSO has reported an EPS of Rs23.83 in 1HFY10.

Other Income surprise!

Other income posted an unexpected growth of 362%YoY mainly due to Rs2.1bn interest income booked by PSO from HUBCO and KAPCO. PSO has charged KAPCO an interest rate of KIBOR+6% while for HUBCO it is approximately 250bps lower. As per PSO's management, a further Rs7bn interest income can possibly be booked in the coming quarters. In line with our expectations, company has reversed Rs265mn of provision of PIA.

Financial charges continue to hurt

Financial charges continued to dent the earnings for PSO as they jumped 33%YoY to Rs3.9bn mainly on account of heavy reliance on short term borrowing to meet its working capital requirements. As of Feb 16, PSO's receivables stood at Rs92.4bn (HUBCO: Rs34.2bn, KAPCO: Rs18bn, WAPDA: Rs38.4bn and PIA: Rs1.8bn). Moreover, PSO has charged interest expense in its books on account of money owed to refineries. A further interest expense of Rs4bn on the same account can be charged, according to the management.

Outlook: 'Buy' maintained

On the back of the 1HFY10 result, we are revising up our earnings estimates by 14%-3% for FY10E and FY11F, respectively, and thus raising our target price to Rs390 from Rs380 earlier. With furnace oil sales already up 25%YoY in the 7MFY10 and 4,500MW of RPPs and IPPS still to be commissioned, we believe there remains a further upside to FO sales growth. However, despite recent hikes in the power tariff, inter-corporate debt remains a concern for PSO. Trading at a FY10E and FY11F PE of 5.8x and 5.0x, respectively, we maintain our 'Buy' stance on the scrip.

Table: Earnings revision

(Rs/share)	Old	New	Δ%
FY10E	45.7	52.2	14%
FY11F	58.9	60.8	3%

Source: JS Research

Also in focus**HBL 2009 earnings preview**

Habib Bank Limited (HBL) is expected to announce its full year earnings on Feb 19, 2010. We expect the company to announce unconsolidated earnings of Rs11.7bn (EPS Rs12.8) as against earnings of Rs10bn (EPS Rs10.98) in the corresponding period last year, an increase of 17%YoY. In 4Q alone, HBL is expected to report a PAT of Rs1bn (EPS Rs1.13), dragged by a one time impairment hit from its investment in Nigeria's Platinum Habib Bank (PHB) worth Rs2.8bn. To recall, PHB reported a loss of US\$2.5bn for the 15 month period ending Sep 2009, of which HBL's share stands at ~Rs13bn. Although this will affect the consolidated accounts, the bank will have to test for impairment on its unconsolidated financials in accordance with IAS 36. Ignoring this event, earnings for 4Q are expected to arrive at Rs3.3bn (EPS Rs3.6). We expect the company to announce a final cash dividend of Rs4/share and do not rule out a bonus issue.

Core operations of the bank are expected to remain strong with Net Interest Income growth of 17%YoY, however Non interest income is expected to drop by 6%YoY. We currently maintain a 'Hold' stance on the scrip.

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