

July 22, 2010

## Pakistan Market

## SHEL: 2Q result to show improvement – HOLD

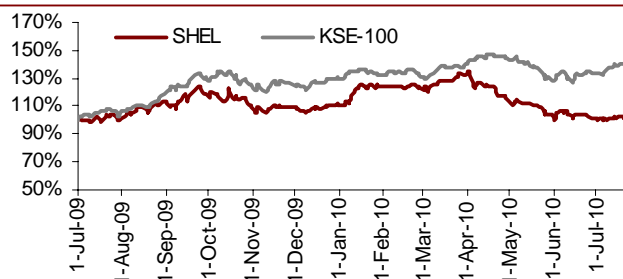
MORNING BRIEFING



KSE100 Index: Closing 10234.03 ↓ (-17.50)

We expect Shell Pakistan (SHEL) to post earnings of Rs7.4/share in 2Q2010, up 27% from the previous quarter. However, we highlight possible tax related issues as a key downside risk to our estimates. With the scrip offering a potential upside of 6% to our DDM based target price of Rs245, we have a 'Hold' stance on SHEL. Moreover, we have taken this opportunity to revise up SHEL's 2010-13 earnings forecast by 14-21% on the back of higher than expected volumetric sales.

## SHEL's relative performance to the market



Source: KSE

## FO sales lift 2Q volumes to 606k tons

SHEL's volumetric sales in 2Q2010 witnessed an increase of 6%QoQ primarily driven by a surge in furnace oil (FO) sales, which were up by a massive 534%QoQ. We believe higher FO sales during the period have been due to the start of fuel supply to Nishat Power. Now with Nishat Chunian Power's (SHEL being its sole fuel supplier) Commercial Operations Date (COD) also achieved on July 21, 2010, we expect FO sales to pick up further, going forward. Motor Gasoline sales too increased during the period by a mere 4%QoQ to 120k tons. On the contrary, sales of high speed diesel, kerosene oil and aviation fuel declined by 5%, 1% & 12%, respectively.

## 2Q earnings to improve; tax remains a concern

We expect 2Q earnings to arrive at Rs7.4/share, 27% higher than the previous quarter on the back of 6%QoQ increase in volumetric sales and 5%QoQ rise in margins of regulated

products, while we anticipate flat margins for the lubricant business. Downside risk to our earnings estimate for the quarter remains, as a result of the abnormally higher tax rate (45%) charged in the previous quarter.

## SHEL's quarter sales

('000 tons)	2Q2010	1Q2010	%Δ
Mogas	120.3	115.3	4%
SKO	2.7	2.7	-1%
JP	110.5	125.4	-12%
HSD	298.5	315.2	-5%
FO	73.9	11.7	534%
Total	606	570	6%

Source: JS Research

## Earnings revised up 14-21% for 2010-13

On the back of higher than expected volumetric sales, we are revising up our earnings estimates by 14-21% for the period 2010-13. We now expect the company to post EPS of Rs29.5 (Rs24.3 earlier) and Rs32.6 (Rs27.6 previously) in 2010E & 2011F, respectively. However, the raise in minimum tax rate to 1% from 0.5% in the Budget FY11 is a major concern for the company's earnings. We believe our earnings estimates (see table below) could erode by 56-59% on account of this increase in minimum tax rate. Our discussions with industry experts have led us to believe that the tax structure is likely to revert back to its previous level of 0.5%.

## SHEL - Key statistics

	2010E	2011F	2012F
EPS (Rs)	29.5	32.6	32.3
Dividend yield (%)	12%	13%	14%
PE (x)	7.8	7.1	7.1
Price to book (x)	2.5	2.5	2.5

Source: JS Research

## Recommendation: 'Hold'

The scrip trades at a 2010E PE and dividend yield of 7.8x and 12%, respectively. At current levels, the scrip offers a potential capital upside of 6% and therefore, we recommend a

'Hold' stance on the scrip.

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## Shell Pakistan Limited

<b>Market Price:</b> Rs230.91	<b>Kats Code:</b> SHEL
<b>Market Cap:</b> Rs15.8bn (US\$185mn)	<b>Bloomberg Code:</b> SHEL PA
<b>1-yr Avg. Daily Volume:</b> 0.1mn shares, Rs25.8mn (US\$0.3mn)	<b>Reuters Code:</b> SHEL.KA
<b>1-year High/Low:</b> Rs307.33/226.09	

## Also in focus

## Cement dispatches up 9% from last year

All Pakistan Cement Manufactures Association (APCMA) has released cement dispatches data for FY10. Local sales arrived at 23.5mn tons, up 14.6%YoY while exports witnessed a slight decline of 1%YoY at 10.7mn tons. Hence, total dispatches for the industry increased to 34.2mn tons as against 31.3mn tons last year, up 9%. Looking ahead in FY11, we expect local sales to improve by 10% on the back of higher Public Sector Development Program (PSDP) utilization while exports to sustain at the levels of 10.5-11mn tons. At current levels, we maintain our 'Buy' call on Lucky and DG Khan Cement.

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