ARIF HABIB LIMITED

Detailed Sector Report

November 11, 2010

Exploration & Production
Exploring Returns

Executive Summary

We reiterate our overweight stance on Pakistan E&P sector with a BUY recommendation on PPL and POL and a SELL stance for OGDC. At the current price level, POL and PPL are offering an upside potential of 24% and 23% based on June'11 target price of PKR 317.2/share and PKR 235.3/share, respectively. OGDC on the other hand, is trading at a premium of 16% to our June'11 target price of PKR 132.6/share. POL and PPL are offering attractive dividend yields of 10.5% and 7.8%, respectively based on our FY11 earnings estimates.

E&P sector is projected to register a 27% YoY earnings growth in FY11

We believe that FY11 would be a better year for the E&P companies compared to FY10. According to our estimates AHL E&P universe is anticipated to post an earnings growth of 27% on account of rising crude oil prices and production growth. Earnings growth will be mainly derived from PPL and POL, which are estimated to post a rise of 41% and 27%, respectively.

Oil and Gas production is likely to grow by 9% and 6%, respectively in FY11

We expect that the crude oil production to post a growth of 9% YoY to 26mn barrels (bbls) in FY11 mainly on account of production enhancement from Mela, Sinjhoro, Maramzai and Mamikhel fields. Similarly gas production is anticipated to rise by 6% YoY to 4,300mmcfd in FY11. The production enhancement of 215mmcfd would come from Maramzai, Mamikhel, and Sinjhoro and Qadirpur fields.

Petroleum Policy 2009 provides a 36% higher gas price compared to 2001

After the failure of 2007 policy, new pricing slabs up to US $100/barrel are introduced in this policy in contrast to 2001 where there was a cap at US $36/barrel. At the current crude price level of $80/barrel, the new policy provides a 36% higher gas prices compared to 2001 policy excluding zonal discounts.

Local E&Ps stand out amongst the regional peers

Due to strong fundamentals and healthy future prospects, all the three listed E&P companies stand out among the regional players on different valuation parameters. On average E&P sector is trading at one year forward PER and PBV of 8.0x and 2.6x respectively, implying a discount of 40% compared to its peers. Furthermore, ROE and dividend yield of 34.7% and 7.4%, implying a premium of 56%.

Debt could be a threat for the E&Ps during FY11

Pakistan E&P sector is deleveraged at the moment. However, the inter-corporate debt issue in the energy chain has severely impacted the E&P's dividend paying capacity. Average dividend payout ratio of E&P companies in AHL universe stood at 53% in FY10 compared to 70% over the past three years (FY07-FY09). Going forward, if the issue is not dealt timely, OGDC and PPL could be forced to seek external financing. However, POL seems comfortably placed and most likely to stay unleveraged.

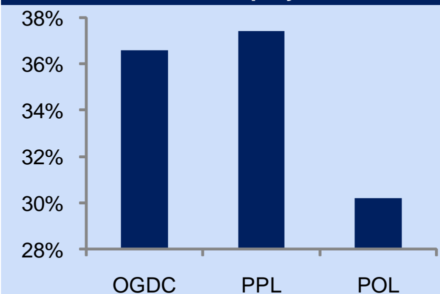
	EPS		PER		Div		Div Yield			
Company	FY11E	FY12F	FY11E	FY12F	FY11E	FY12F	FY11E	FY12F	TP	Stance
OGDC	15.0	16.3	10.6	9.7	6.0	7.0	3.8%	4.4%	132.6	Sell
PPL	27.5	30.3	7.0	6.3	15	16	7.8%	8.3%	235.3	Buy
POL	39.8	43.6	6.4	5.9	27	29	10.5%	11.3%	317.2	Buy

Source:AHL estimates

Overweight

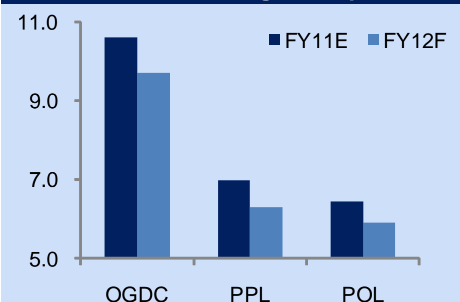
Company	Target price	Stance
POL	317.2	Buy
PPL	235.3	Buy
OGDC	132.6	Sell

Return on Equity FY11F



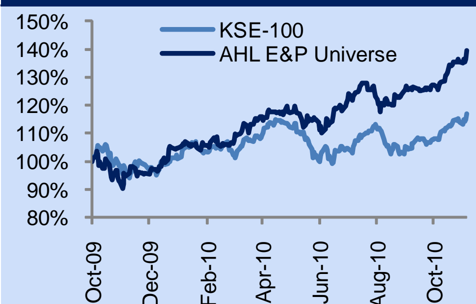
Source: AHL Research

Price to Earnings Multiple



Source: AHL Research

Relative Price Performance



Source: KSE

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Insatiable energy demand is keeping E&Ps in the driving seat

Pakistan energy demand has grown at a CAGR of 8.4% during FY2006-10, outpacing the GDP growth rate of 6.4% for the same period. Owing to the strong correlation between energy consumption and economic growth, coupled with huge supply demand deficit, we expect that the energy demand to grow at a CAGR of 6% during FY2011-2015.

Currently, Pakistan satisfies 81% of its primary energy needs through oil and gas. Total demand of oil and gas in Pakistan stands at 51mn tonnes of oil equivalent (Toe) whereas, current production is 34mn toe and the rest is met through imports. Recoverable oil and gas resource potential of Pakistan has been estimated at 27bn bbls of oil and 282 trillion cubic feet (tcf) of gas. As per the estimates, only 3% and 19% of respective oil and gas reserves have been discovered so far in Pakistan.

We believe that the E&P companies are well positioned to reap the benefits of growing energy demand and huge hydrocarbon potential. Strong balance sheets and favorable regulatory framework may help the local E&P companies to enhance their exploration/development activities.

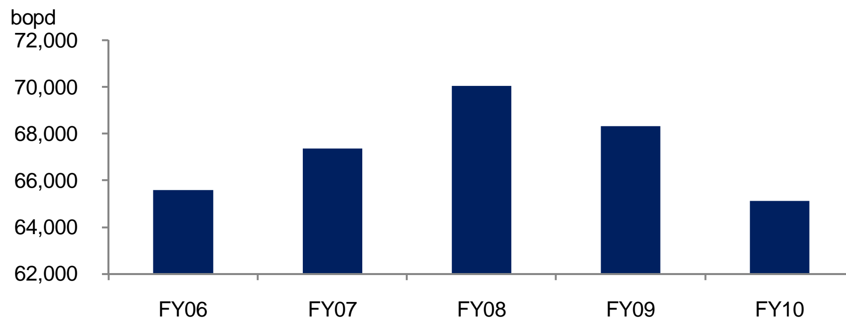
Current oil and gas reserves are expected to last for the next 13 and 19 years, respectively

Pakistan is still in the initial stage of exploration with one of the lowest drilling density of 2.09 wells/1,000 sq km and a higher success ratio of 30%. As of Dec'09, E&P activities in the country have resulted in original recoverable reserves of 947 mn barrels of oil and 54 tcf of gas. Out of which, 303 mn barrels of oil and 28 tcf of gas are balance recoverable reserves. At the current production rate, Pakistan current oil and gas reserves would fully deplete in the next 13 and 19 years, respectively assuming no further discovery.

Crude oil production is expected to bottom out in FY10

Oil production after recording a rise of 3% YoY and 4% YoY in FY07 and FY08, respectively; has witnessed a slide of 6.7% YoY and 6.9% YoY in FY09 and FY10, respectively. This is on account of natural depletion from major fields like Chanda, Kunar and Pindori, which contribute approximately 35% to 40% of the total oil production in Pakistan. Average oil production for FY10 was recorded at 65,123 bopd.

Crude oil production



Source: PPIS

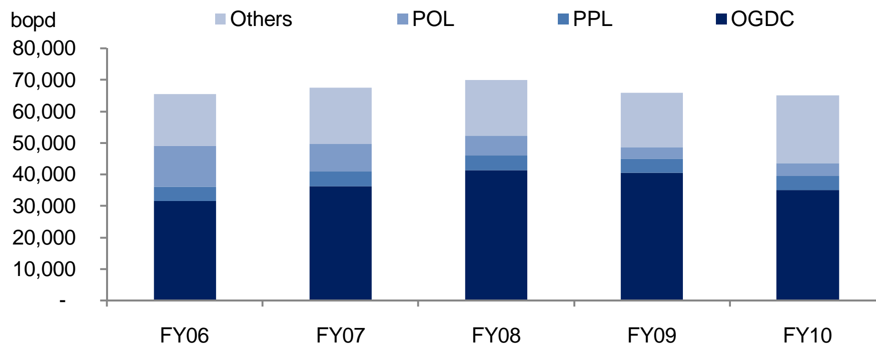
New fields, which came online in FY10, were Manzalai of Tal block, Adam, Bela and Naspha. Manzalai started commercial operations in 2QFY10; contributing a decent 8% towards the total oil production in FY10.

On a company wise basis, OGDC produced 35,004 bopd in FY10, which is below its 4 year average of 39,971 bopd. This is primarily due to decline in production from Chanda, Sono, Dakhni, Kunar and Mela fields, which contribute almost 60% to OGDC's total oil production. However, Adhi and Thora (contribution 9%) recorded an improvement in oil production of 4% YoY and 16% YoY, respectively.

During FY10, PPL produced 4,533 bopd compared to 4,130 bopd in the corresponding period last year, marking an improvement of 10% YoY. Increase in oil production from Adhi field by 4% and commencement of Manzalai field in Nov'09 were the main contributor towards rise in PPL's production.

POL remained the major beneficiary in terms of crude oil production growth in FY10. Its production showed a healthy growth of 8% to 4,103 bopd from 3,792 bopd exhibited in the same period last year. The reason for this growth was commencement of Manzalai field, which is currently yielding 4,000 bopd where POL's stake is 21%.

Crude Oil production



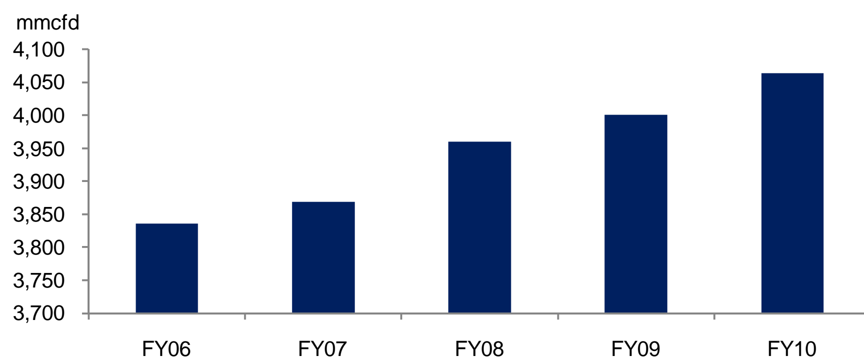
Source: PPIS

We expect that the average crude oil production to post a growth of 8%-9% YoY to 71,233 bopd in FY11 mainly on account of production enhancement from Mela, Sinjhoro, Maramzai and Mamikhel fields. The production enhancement from these fields would be 3,500, 3,000, 600 and 1,500 bopd, respectively.

Gas Production is expected to record a growth of 6% YoY

Over the past five years (FY06-FY10) gas production has grown at an average rate of 1.45% per annum to 4,060 mmcfd. This modest increase is a result of sluggish growth witnessed in major producing fields such as Mari and Kandkhot, which contribute 16% to the total gas production of the country. However, during the same period some other fields such as Miano, Sawan and Sui (25% contribution to total gas production of the country) have recorded a decline. The average gas production stood at 4,060 mmcfd during FY10 compared to 4,000 mmcfd in FY09, showing a modest increase of 1.6% YoY. The contribution of gas production by PPL, OGDC and POL remained at 23%, 22% and 1%, respectively in FY10.

Natural Gas production



Source: PPIS

The gas fields, which came online in FY10, were Manzalai from Tal Block and Adam-1 from Hala Block. Working interest in Manzalai is 27.8% each for OGDC and PPL whereas for POL it is 21.1%. Adam-1 is 65% owned by PPL and 35% by Mari Gas. In FY10, contribution from Manzalai and Adam-1 remained at 4.4%. In FY11 we expect that the contribution to total gas production from these fields to rise to 6% on account of full year impact of these fields.

Mari gas field, which contributes 12% to total gas production of Pakistan, has exhibited an average growth of 6% in the past five years (FY06-FY10) and 13% YoY in FY10. On average it produced 495 million cubic feet of per day (mmcfd) for FY10. Qadirpur, which contributes 12% to total gas production of Pakistan, posted a decline of 9% YoY in FY10 whereas from FY06 to FY10 its production has remained stagnant at around 480 mmcfd. Gas production from Sui posted a decline of 6% YoY in FY10 and 17% on average over the last five years. In FY10 its production hovered around 562 mmcfd compared to 677 mmcfd recorded in FY06.

OGDC gas production in FY10 stood at 898 mmcfd compared to 932 mmcfd in FY09, recording a decline of 4% YoY. This decline mainly emanated from Qadirpur and Uch gas fields, which cumulatively contribute 62% towards the total gas production of OGDC.

PPL gas production stood at 943 mmcfd in FY10 compared to 965 mmcfd recorded in FY09, registering a decline of 2% YoY. The attribute for this decline is a 6% YoY production drop from Sui gas field, which contributes around 60% (562mmcfd) of the company's gas production.

FY10 was a year of turnaround for POL as its gas production exhibited an unprecedented rise of 60% YoY to 60mmcfd. The cause for this phenomenal rise was Manzalai field, which came online in Nov'09. Currently, this is contributing two-third of total gas production of the company.

We expect that the gas production to post a growth of 6% YoY 4,300 mmcfd in FY11. The production enhancement of 215 mmcfd would come from Maramzai, Mamikhel, Sinjhoro and Qadirpur fields. The production additions from these fields would be 20, 20, 25 and 150 mmcfd, respectively.

Huge untapped potential will open up opportunities for E&Ps

Pakistan has onshore and offshore sedimentary area of 827.3km^2. The recoverable oil and gas resource potential of Pakistan has been estimated by Pakistan Petroleum Information Service (PPIS) at 27bn barrels of oil and 282 tcf of gas. Only 3% of the estimated oil and 19% of the natural gas potential resources have been

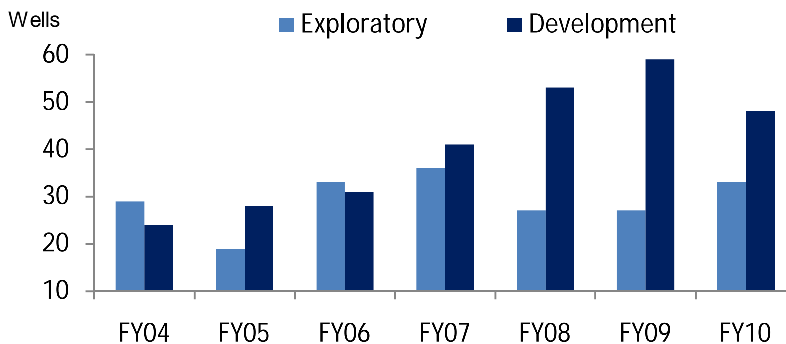
discovered so far in Pakistan from 743 exploratory wells over the past 63 years. This suggests only minor portion of the hydrocarbon reserves have been discovered so far and a gigantic portion has yet to be discovered. For on-shore West Baluchistan and Potohar Basin (Zone-1) and for off-shore Indus Basin offers a huge potential. Therefore, E&P sector would benefit if any hydrocarbons are discovered from these zones.

Exploration activity has picked up

To date, 743 exploratory wells and 990 development/appraisal wells have been drilled in Pakistan. A total of 68 and 150 oil and gas discoveries respectively, have been made till now. This translates into an overall exploratory success ratio of 1:3.4 wells. A 5 year average comparison shows that during FY06-10, 64 wells were drilled compared to 47 well during FY01-05. A total of 57 discoveries (mainly gas/ condensate) were made during FY05-FY10.

This is indicative of a rise in drilling activity over the last 5 years on the back of higher FDI investment and rising gap between demand and supply. On account of oil deficit, investor friendly petroleum policies and high success ratio, we foresee exploration and development activities to pace up going forward.

Exploration and Development Activity



Source: PPIS, AHL Research

Fifth major discovery in TAL Block

MOL, a Hungarian based company, has recently announced discovery from its exploratory well Makroi East -1, at TAL block. The TAL block is located in NWFP and some area of FATA. It covers area of Kohat, Karak, Hangu, Bannu, North Waziristan and Orakzai agencies. This is fifth major discovery in TAL block, which includes Manzalai, Makori, Mamikhel and Maramzai. According to company's notice, initial test showed that the well has produced oil of 3,209bbls/day and 10.7 mmcfd of Gas. Currently, the well has reached 84% of its target depth and full extent of discovery fill be evaluated after reaching target depth of 4,169 meters, which is expected in next 3 months. We expect the production flows from the field to commence from FY12.

OGDC and PPL each holds 27.8% stake in TAL block while share held by POL is 21.1%. Based on initial flows, POL is expected to be the major beneficiary of this discovery on account of its low equity and production base with after tax impact of PKR 3.70/share. While the impact on PPL and OGDC's bottomline is expected to be around PKR 1.17/share and PKR 0.27/share.

A view of TAL Block

Source: MOL

Petroleum Policy 2009 provides a 36% higher gas price compared to 2001 Policy

The government revealed the new Petroleum Policy 2009 on March 20, 2009. After the failure of 2007 policy, new pricing slabs up to US $100/barrel are introduced in this policy in contrast to 2001 where there was a cap at US $36/barrel. At the current crude price level of $80/barrel, the new policy provides a 36% higher gas prices compared to 2001 policy excluding zonal discounts. The government is diligently marketing the investment proposal of the new policy to foreign investors and has organized several conferences to attract more foreign investment in Pakistan E&P sector. We believe that the presence of foreign players is vital as this would not only bring in competition making local players more pro-active but also partnership opportunities will be opened, which would result in rise in profitability of local players.

Tight Gas Reserves Policy will add to potential reserves

Ministry of Petroleum and Natural resources (MPNR) revealed a draft policy regarding Tight Gas Reserves (TGR). The objective of this policy is to open new frontiers for exploration of tight gas from the existing gas reservoirs. This policy will aid in meeting 6% per annum energy demand growth. TGR policy is silent on the tax rate to be charged on the income generated on tight gas. According to OMV study, tight gas potential is in the vicinity of 33 to 40 (tcf) located in upper Indus Basin and Kirthar. This is 18%-43% higher than the Pakistan's current recoverable reserve balance of 28 tcf.

What is Tight Natural Gas

Tight gas is stuck in a very tight formation underground, trapped in unusually impermeable, hard rock, or in a sandstone or limestone formation that is unusually impermeable and non-porous. Extraction of this gas requires advanced technology, which essentially would result in total Capex requirement of around US$23 million/well versus capex of US$15mn needed to spud a conventional well and Permeability (gas flow rate) is less than 1 milli Darcy (mD)

Key proposals of this policy are as follows:

- A 40% premium on top of zonal prices computed under 2009 Petroleum Policy. A sweetener in the draft is an additional 10% premium on gas prices for those volumes that are brought into production within 2 years of announcement of this policy.

- Royalty will be payable as per Petroleum Policy 2009 (12.5%)
- No windfall levy will be applicable to the tight gas production
- Restriction on commingled (tight gas or conventional gas produced from the same well) production.

Comparison of wellhead prices of a conventional well and TGR well is given in the table below:

Normal Gas Prices (US$ per mmbtu)				
Crude Oil	Zone 0	Zone I & offshore shallow	Zone II	Zone III
US$ per barrel				
Upto 20	2.89	2.72	2.54	2.37
Above 20 to 30	3.62	3.40	3.18	2.96
Above 30 to 40	4.05	3.81	3.56	3.32
Above 40 to 70	4.92	4.62	4.32	4.03
Above 70 to 100	5.36	5.03	4.71	4.38
TGR gas prices				
Crude Oil	**Zone 0**	**Zone I & offshore shallow**	**Zone II**	**Zone III**
Upto 20	4.05	3.81	3.56	3.32
Above 20 to 30	5.07	4.76	4.45	4.14
Above 30 to 40	5.67	5.33	4.99	4.64
Above 40 to 70	6.89	6.47	6.05	5.64
Above70 to 100	7.50	7.04	6.59	6.13

Sources: Petroleum Policy 2009 & TGR draft policy

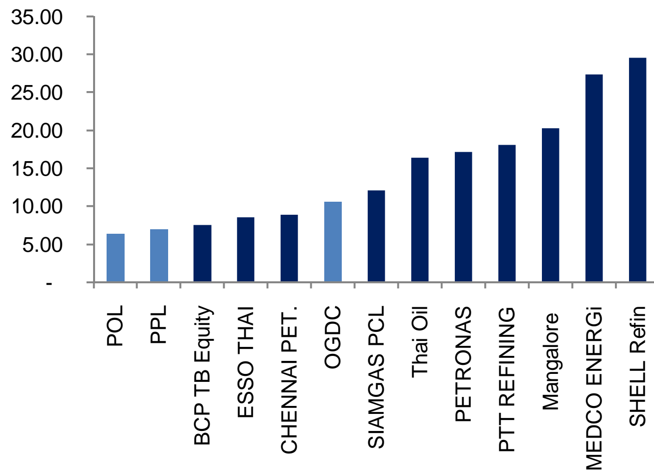
More enticement is required

In our view, E&P operators will demand better incentives for extracting tight gas such as better pricing, lower royalty and reduced tax rate due to the difficulty and higher cost affiliated with extraction. However, we believe that this to be a step in the right direction, which will aid in enhancing hydrocarbons and meeting our energy requirements. Moreover, this policy will open new opportunities for investments and will add towards the gas reserves. While the TGR is highly concentrated in Sindh Province, we anticipate the primary beneficiaries to be PPL and OGDC. The key concern here remains the implementation of new technology and skill, which could give foreign E&P companies an upper-hand over local companies. Currently, out of 26 E&P operators, 10 are local and rests are foreign.

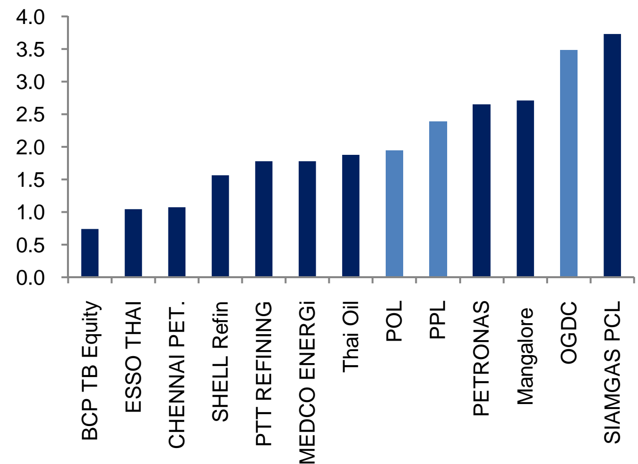
Local E&Ps stand out amongst the regional peers

Due to strong fundamentals and healthy future prospects all the three listed E&P companies stand out in comparison with regional players on different valuation parameters. On average E&P sector is trading at one year forward PER and PBV of 8.0x and 2.6x respectively, implying an average discount of 40% compared to its peers. Furthermore, ROE and dividend yield of 34.7% and 7.4%, respectively implying an average premium of 56%.

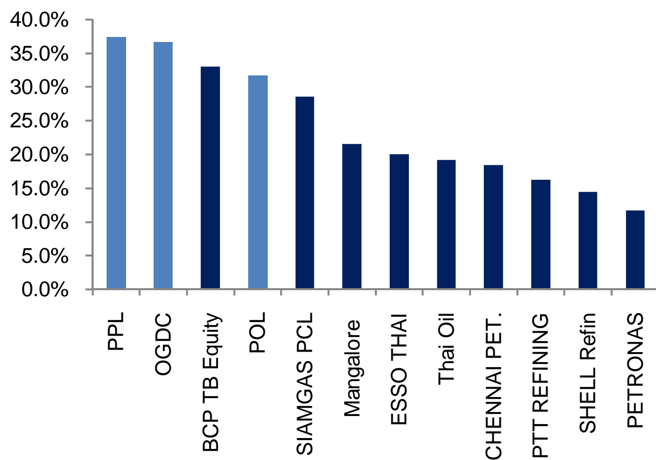
Estimated PERx for FY11



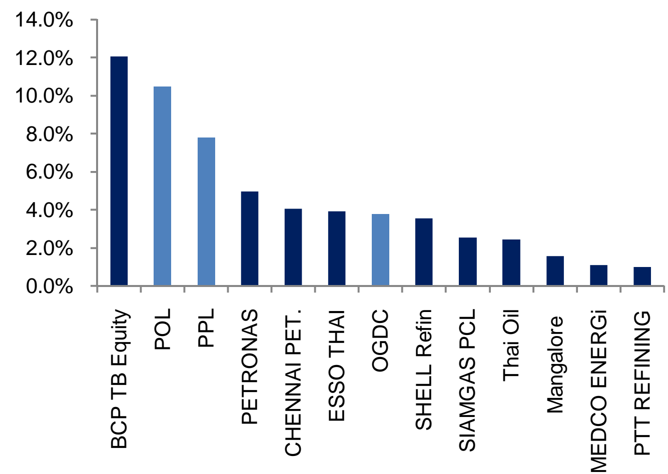
Estimated PBV for FY11



Estimated ROE for FY11



Estimated Yield for FY11



Source: AHL Research, Bloomberg

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Price outlook for crude oil

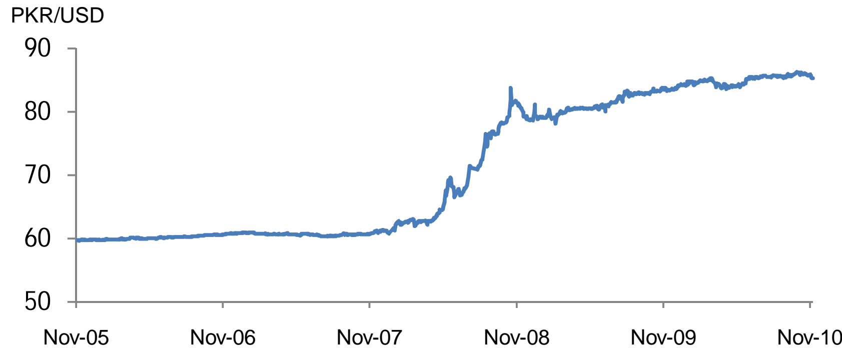
Before the economic meltdown in September 2008, the crude oil price touched US$147 a barrel and then dropped to around US$33 a barrel in January 2009. Currently, the oil prices have been moving in a range of US$75-85 a barrel for the last 12 months. Given the global economic growth to reach 2%-2.5% in FY11, we expect that the oil demand and prices to pick up. Another reason for higher price going forward is the increasing marginal cost of extraction, which has jumped from US$5-6 a barrel in 1980s to around US$15-20 a barrel due to the higher extraction cost required for difficult fields. We expect that the crude oil prices to improve gradually from FY11. The average Arab Light price for FY11 is expected to be US$75 while we foresee on average the Arab Light to reach US$80 a barrel during FY12 and FY13.

E&Ps are a hedge against PKR Depreciation

E&P returns are hedged against PKR depreciation, so we believe that investing in these stocks is ideal for those who want to hedge their return against PKR depreciation. Pricing of crude oil produced in Pakistan is pegged with Arab Light crude prices quoted in US Dollar terms. Similarly, wellhead gas prices of discoveries of post 1994 are also linked with Arab Light crude prices, whereas for older fields (Pre 1994 discovered) gas prices are linked to international High Sulphur Furnace Oil (HSFO) prices, which are also in US dollar terms.

With devaluation in PKR against the US Dollar, E&P sector stands out as the major beneficiary. Sector's earnings and the target prices of the companies in the AHL E&P universe are expected to surge by 3%-4%, for every 1% depreciation in PKR against the US dollar. In FY11 we expect that the Greenback may appreciate by 3% against the PKR.

PKR depreciation against USD



Source: SBP

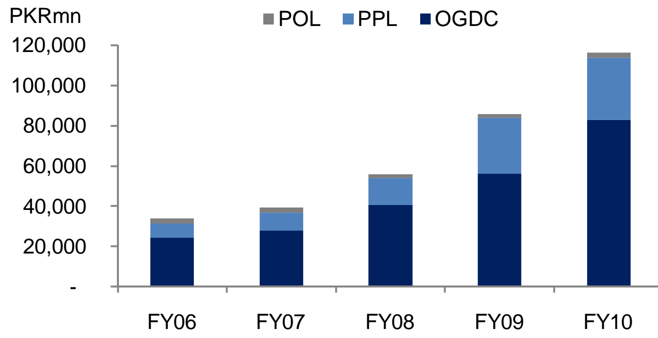
Debt could be a threat for the E&Ps

Pakistan E&P sector is deleveraged at the moment. Historically all E&P companies have generated sufficient funds to cater their capital expenditures and working capital requirements. However, the inter-corporate debt issue in the energy chain has severely impacted the E&P's dividend paying capacity. Average dividend payout of E&P companies in AHL universe stood at 53% in FY10 compared to 70% over the past three years (FY07-FY09). The total trade debts of OGDC, PPL and POL have aggregated to PKR 116bn as at June'10, depicting a surge of 35% YoY.

So far the government has not been able to resolve the issue, despite the floating of TFCs worth PKR 162.4bn in two phases, gradually increasing power tariff and eliminating oil subsidies. Recent actions like dissolution of PEPCO and plans for further power tariff hike are some measures to ease the intensity of circular debt. Besides, interest from the foreign donor's institutions (IMF and World Bank) in resolution of circular debt is painting a rosy picture on the energy canvas of the country. We do not see a complete resolution of circular debt, however above mentioned remedies may reduce circular debt to a sustainable level.

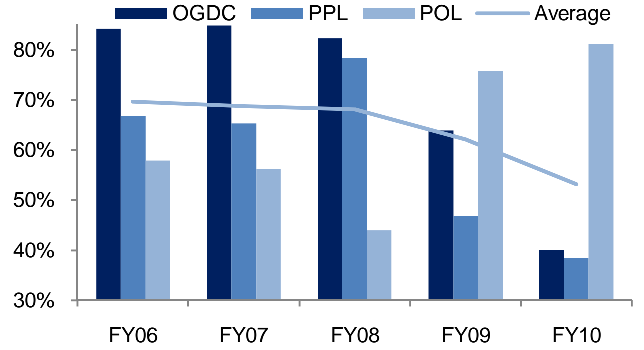
Going forward if the issue is not dealt timely, we see a medium term probability of OGDC and PPL seeking external sources to meet their capital expenditure requirements. However, POL seems comfortably placed and will most likely stay unleveraged as most of POL's oil is supplied to Attock refinery, a group company which has historically paid its dues promptly.

Rising Trade Debts



Source: Company accounts, AHL Research

Dividend Payout



Source: Company accounts, AHL Research

ARIF HABIB LIMITED

Company Report

November 11, 2010

Oil & Gas Development Company Limited — Oil and Gas

All positives are priced in

OGDC is currently trading at FY11E PE multiple of 10.6x, a premium of 32% over the sector. Furthermore, the scrip is trading at a premium of 16% based on our June 2011 reserve based target price of 132.6/share. Thus, we recommend Sell for the scrip as all the positives seems to be priced in at current levels.

Solid product mix is hedging against oil price volatility

The Company's revenue mix is expected to further tilt in the direction of natural gas with revenue contribution from gas expected to increase to 71% in FY15 from 53% in FY10 this is on account of rise in gas production from development fields such as Dakhni, Jhal Magsi and Uch. Increased gas revenues are expected to provide further stability to OGDC's earnings, by lowering sensitivity to oil price movement.

Circular debt is posing a threat to payout

Company's cash position is deteriorating fast owing to the notorious circular debt issue prevailing in the energy chain since the past few years. If trade debts perpetuate to move in the north direction and cash in the south direction then this may become a big barrier for company's vigorous exploration program and dividend payout may be curtailed further.

Positive development on Qadirpur is likely to bode well for OGDC

Installation of fourteen compressors to halt the "natural gas depletion" of the premier field, Qadirpur, which contributes about 38%-40% to total gas production of the OGDC has been completed. Installation of these gas compressors is likely to improve gas yield from current level of 486 mmcfd to 650 mmcfd till December 2010.

Risks

The major risks associated with OGDC are fluctuations in crude oil prices, exchange rate risk and project delays.

Financial Highlights

PKRmn	FY09A	FY10A	FY11E	FY12F	FY13F
Revenues	130,830	142,572	160,950	171,524	193,453
Net Profit	55,540	59,177	64,317	70,846	81,201
Shareholders' Equity	126,171	157,392	195,909	236,656	283,456
Total Assets	177,992	228,868	269,254	312,321	361,542
EPS (PKR)	12.92	13.76	14.96	16.48	18.88
DPS (PKR)	8.25	5.50	6.00	7.00	8.00
BVS (PKR)	29.34	36.60	45.55	55.02	65.91
PER x	12.26	11.51	10.59	9.61	8.38
Dividend Yield	5.2%	3.5%	3.8%	4.4%	5.1%
PBV x	5.40	4.33	3.48	2.88	2.40
Net Margin	42.5%	41.5%	40.0%	41.3%	42.0%
ROA	31.2%	29.1%	25.8%	24.4%	24.1%
ROE	44.0%	41.7%	36.4%	32.8%	31.2%

Sources: Company accounts, AHL estimates

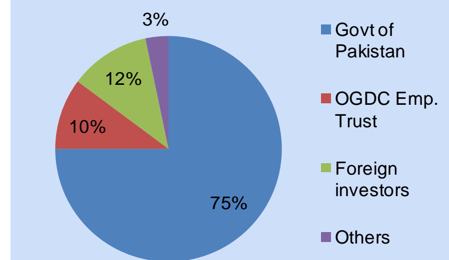
Sell

Target Price (PKR/share)	**132.6**
Last Closing (PKR/share)	**158.3**
Downside	-16.3%
KSE Code	OGDC
Bloomberg Code	OGDC PA
Reuters Code	OGDC. KA

Key Data

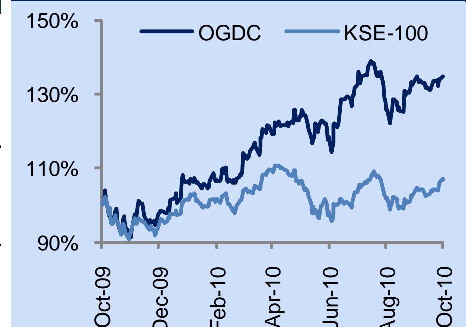
Outstainding Shares (mn)	4,300.93
Market Cap (US$ mn)	7,918.71
Market Cap (PKR mn)	681,009.0
Free Float	15%
12M Avg. Daily Turnover	2.8mn
12M High/Low (PKR)	158.34/100.27

Shareholding



Source: Company accounts

Stock Performance



Source: Bloomberg

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Valuation

We have revised our reserved based June'11 target price for OGDC to PKR 132.6/share. At last closing price of PKR 158.34/share, the stock of OGDC is trading at a premium of 16%, thus we recommend Sell. Our valuation is derived from cost of equity of 19.8%, based on risk free rate of 13.5% and beta of 1.1.

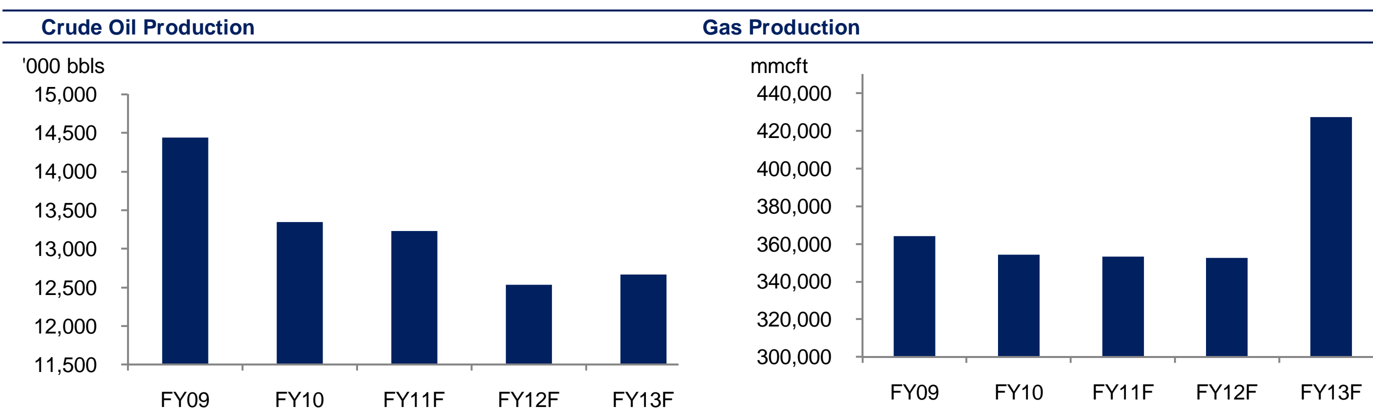
Valuation Summary

FY10 end oil reserves (mn barrels)	235
FY10 end gas reserves (bcf)	13,833
Total Reserves (mnboe)	2,541
Present value of reserves (PKRmn)	551,403
Exploration Upside	-
Debt	-
Cash & cash equivalents (PKRmn)	18,920
Investment in subsidiary (PKRmn)	2,880
Reserved based value (PKRmn)	570,323
Shares Outstanding (PKRmn)	4,300
Target Price (PKR/share)	132.63

Source: AHL research

Oil production is expected to decline whereas gas production is likely to post a major increase

The company's oil production is expected to decline at an average rate of 2% per annum from 13.34mn bbls in FY10 to 13.10mn bbls in FY14 (assuming no discovery). This is mainly on account of decline in production from major producing fields like Chanda, Dakhni and Pasakhi, which cumulatively contribute about 25% in total oil production of the company. However, gas production is anticipated to grow at a CAGR of 4% for the same period. We believe that the gas production would rise to 407,573 mmcft in FY14 from 354,327 mmcft witnessed in FY10. This staggering rise would be on account of rise in production from Mamikhel, Kunar, Uch and Qadirpur.



Source: Company Accounts, AHL Research

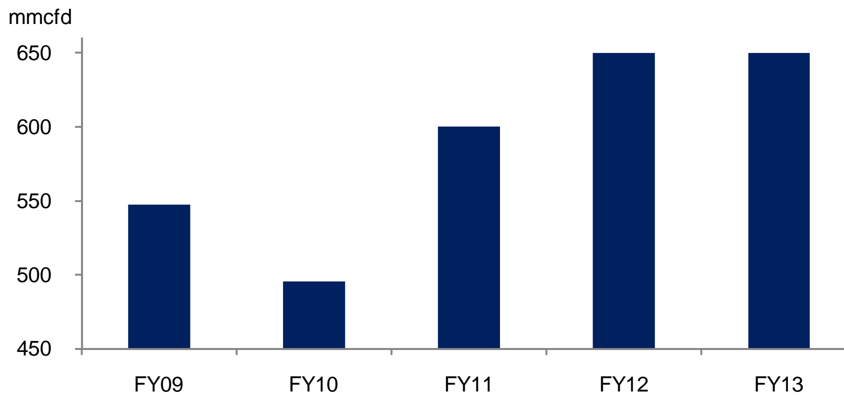
Source: Company Accounts, AHL Research

Positive Development on Qadirpur is likely to bode well for OGDCL

Installation of fourteen compressors to halt the "natural gas depletion" of the premier field, Qadirpur which contributes about 38%-40% to total gas production of the OGDC has been completed. Installation of these gas compressors is likely to

improve gas production from the current level of 486 mmcfd to 650 mmcfd till December 2010. After 18 months three additional compressors will be shifted from Pirkoh field to meet compressor requirement till FY14.

Gas production



Sources: PPIS and AHL Research

Vital development projects would arrest the decline in production

OGDC has taken on several development projects on its existing and new fields to arrest decline in total oil and gas production of the company. Following are the vital development projects planned for the next few years, which would play a pivotal role in improving declining company's oil and gas production.

- Uch-2 development: The field is located in Baluchistan province and is currently supplying 250mmcfd to the Uch Power Plant. The company has planned to increase gas production to 410mmcfd from FY14.

- Dakhni expansion: the expansion is estimated to be completed by October'11. It will provide an incremental production of 720 bopd, 12mmcfd gas, and 80 tons of sulphur per day.

- Kunnar and Pasahki Deep/TAY Integrated development project: Currently the process is under litigation. Upon completion, this project will enhance OGDC production by 4,400 bopd, 285 mmcfd of gas and 361 tons of LPG.

Projects	Oil (bopd)	Gas (mmcft)	Target date
Sinjhoro	3,500	25	Jun'11
Qadirpur	-	150	Sept'10
Jhal Magsi	-	15	Mar'12
Uch-11	-	160	-
KPD/TAY	4,400	285	May'12
Dakhni	720	12	Oct'11

Source: Company accounts

The following table shows the earnig impact of different projects

Field	Working Interest	Production addition Oil (bopd)	Gas (mmcfd)	Earnings impact (PKR) Oil	Gas	Total
Uch-2	100%	-	160	-	2.35	2.35
Dakhni	100%	720	12	0.15	0.11	0.26
Sinjhoro	100%	2,100	31	0.45	0.20	0.65
Kunnar/TAY	100%	4,700	278	0.95	1.85	2.80
Naspha	70%	3,500	12	0.55	0.10	0.65
Qadirpur	75%	-	150	-	1.10	1.10

Source: Company accounts, AHL estimates

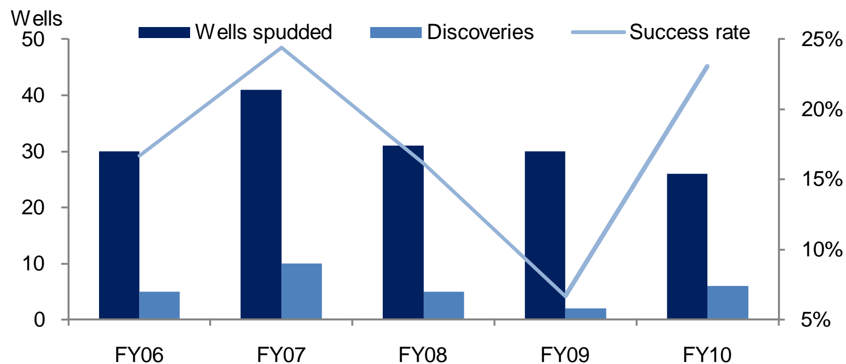
Given the commencement dates of mentioned fields; the above table provides annualized earnings impact on the Company

OGDC exploration plans are ambitious

The widening supply demand gap has induced E&P companies to invest more in exploration and development. OGDC has spent PKR 67 billion in the past five years on fixed capital expenditure reflecting the Company's aggressive exploration stance. Going forward actualization of exploration and development projects will aide in enhancing company's production translating in earnings growth. The Company has even shown intentions of going global with ENI through non-operated joint venture agreement.

OGDC has a drilling and capex target of 48 wells (worth US$800mn) for FY11. Over the past five years the company has drilled an average of 32 wells per annum. Owing to company's massive balance sheet size of PKR 229bn and zero leveraged capital structure, OGDC appears well positioned to take advantage of the potential offered by vast untapped areas for further exploration. However, the drilling and capex target seems a little too ambitious despite company's size, as the inter corporate debt issue will continue to plague the entire energy chain.

Wells Spudded and Discovered



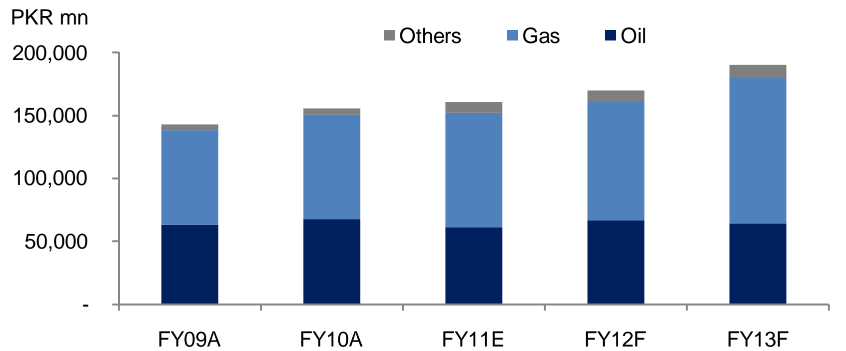
Source: PPIS

Solid product mix is hedging against oil price volatility

OGDC revenue mix is expected to further tilt towards natural gas with revenue contribution from gas to surge to 71% in FY15 from 53% in FY10. This is on account of rise in production from development fields such as Dakhni, Jhal Magsi and Uch. Subsequently share of oil revenues is expect to decline to 25% by FY15 from current standing of 43%. This drop is expected on account of depletion of

major fields like Bobi and Chanda. Increased gas revenues are expected to provide further stability to OGDC, which are less sensitive to oil price movement. Reason is presence of floor and cap in gas pricing formula and using average price following last six months as a benchmark.

Revenue Mix



Source: PPIS, AHL Research

Qadirpur price issue still needs to be resolved

The much awaited price revision (benefit of PKR depreciation) for Qadirpur gas field was allowed lately (Feb'10) for the last four quarters starting from January 2008 to December 2009. Consequently, the company benefited by booking one time retrospective gain of PKR 0.8/share. However, this pricing issue has not been fully resolved. The negotiated discount table for Qadirpur issue stills needs to be approved by The Economic Coordination Committee (ECC). If the Qadirpur disputed price issue is resolved completely, we expect that the Qadirpur gas price would be further revised upwards to PKR 270.15/mmbtu from the current level of PKR 213.17/mmbtu. This rise would increase our earnings and target price on average by 4% from FY11 and onwards.

Revision in Bobi field prices will improve earnings

OGRA for the first time has unveiled the wellhead price for the Bobi field (100% stake owned by OGDC), that contributes on average 1.2% to gas production of the company. The price for the period effective from July'10 to Dec'10 has been set at PKR 382.08 per mmbtu. Based on the field's average gas production level of 12mmcfd, this revision is likely to have an earnings impact of PKR 0.32 per share (includes retrospective impact of PKR 0.26) on OGDC's bottom line in 1HFY11.

Circular debt is posing a threat to payout

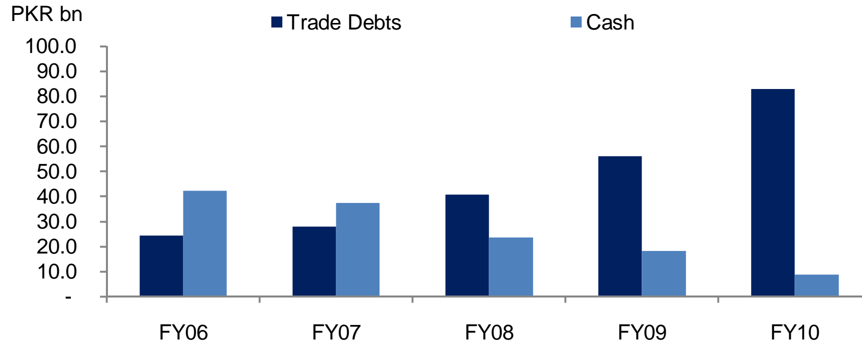
Over the past few years, company's cash rich position has been severely affected due to circular debt issue. As per FY10 accounts, the company has cash and cash equivalents of PKR 19bn compared to PKR 42bn recorded in FY05. This is due to higher trade debt, which has ballooned to PKR 83bn compared to PKR 24bn witnessed in FY05.

In an attempt to manage its cash flows, the company has trimmed down dividend payout ratio from 85% in FY05 to 40% in FY10. Furthermore, the company has withheld royalty payments of Government of Pakistan, which have risen to PKR 16bn, an increase of 3.72x YoY.

In order to reduce the intensity of circular debt the government had issued TFC's worth PKR 162.4bn in two tranches. However, these issued TFC's did not reduce the receivable of the companies as major chunk was consumed by IPPs and OMCs

before it could reach the last recipients. If trade debts perpetuate to move in the north direction and cash in the south direction then this may become a big barrier for company's vigorous exploration program and dividend payout. Dividend payout has been reduced to 40% in FY10 compared to 85% witnessed in FY05. Our dividend payout expectations for FY11E and FY12F is 40% (PKR 6/share) and 43% (PKR 7/share) respectively.

Trade debts and Cash Position moving in opposite direction



Source: Company Accounts

Exchangeable Bond will have a neutral impact on OGDC

As part of the privatization program the Government of Pakistan (GoP) had planned to issue exchangeable bonds of OGDC in the international market few months back but no progress has been seen in this regard so far. The government is expected to fetch around US$500mn by monetizing 5%-7% of its 75% ownership in the company. News reports suggest that the GoP may use these funds either to finance some portion of its fiscal deficit or to decrease the inter corporate debt, which is afflicting the entire energy chain of the country. This will have no impact on the valuation of OGDC's stock.

Summary Financials and forecasts, PKR million except per share data and ratios

Income statement	FY09A	FY10A	FY11E	FY12F	FY13F
Net sales	130,830	142,572	160,950	171,524	193,453
Field Expenditures	(22,674)	(23,728)	(28,166)	(28,301)	(31,920)
Royalty	(15,156)	(16,279)	(18,885)	(20,126)	(22,699)
Other income	3,371	3,300	3,350	3,675	3,822
Profit before taxation	80,928	88,553	96,717	106,536	122,106
Taxation	(25,388)	(29,376)	(32,400)	(35,689)	(40,906)
Profit after taxation	55,540	59,177	64,317	70,846	81,201
Earnings per share (PKR)	12.92	13.76	14.96	16.48	18.88
Dividend per share (PKR)	8.25	5.50	6.00	7.00	8.00
Balance sheet	**FY09A**	**FY10A**	**FY11E**	**FY12F**	**FY13F**
Paid-up capital	43,009	43,009	43,009	43,009	43,009
Shareholder's equity	126,171	157,392	195,909	236,656	283,456
Non current liabilities	30,534	36,634	38,093	39,998	41,998
Current Liabalities	21,287	34,841	35,251	35,667	36,089
Total Liabalities	51,821	71,475	73,344	75,665	78,086
Non current assets	92,532	108,434	124,811	140,685	155,516
Current assets	85,461	120,434	144,443	171,635	206,026
Total assets	177,992	228,868	269,254	312,321	361,542
Cash flows	**FY09A**	**FY10A**	**FY11E**	**FY12F**	**FY13F**
Net operating cash flow	52,979	61,506	79,529	86,048	95,673
Net investing cash flow	(22,910)	(22,839)	(34,000)	(35,700)	(37,485)
Net financing cash flow	(39,406)	(28,770)	(30,100)	(34,400)	(38,700)
Net change in cash	(9,337)	9,897	15,429	15,948	19,488
Cash at the end of the period	3,974	7,844	23,273	39,221	58,709
Ratios	**FY09A**	**FY10A**	**FY11E**	**FY12F**	**FY13F**
Dividend yield	5.2%	3.5%	3.8%	4.4%	5.1%
Return on average equity (ROE)	44.0%	41.7%	36.4%	32.8%	31.2%
Return on assets (ROA)	31.2%	29.1%	25.8%	24.4%	24.1%
Price to earning ratio (PER)	12.26	11.51	10.59	9.61	8.38
Book value per share (PKR)	29.34	36.60	45.55	55.02	65.91
Price to book ratio (PBR)	5.40	4.33	3.48	2.88	2.40
Net profit margin	42.5%	41.5%	40.0%	41.3%	42.0%

ARIF HABIB LIMITED

Company Report

November 11, 2010

Pakistan Oilfields Limited

Oil and Gas

Time to go long

The scrip of POL offers an upside potential of 24% based on June-11 reserved based target price of PKR 317.2/share. Furthermore it is currently trading at an attractive PER and dividend yield of 6.4x and 10.5% based on our FY11 earnings estimates.

TAL forms the heart of our investment case

Production addition from Tal is the heart of our investment case for POL. The company has 21.1% stake in the TAL Block, due to low equity and production base allows POL to benefit the most. Production from TAL is expected to reach 8,600 bopd and 367 mmcfd of gas by Dec'11 as compared to 3,700 bopd and 190 mmcfd of gas recorded in FY10.

Production is likely to increase at a 5-year CAGR of 9.4%

Oil and Gas production of the company is expected to increase at a 5 year CAGR (FY10-FY15) of 9.4% from 5.2mn boe to 7.3mn boe, mainly attributed to flows from TAL block. FY11 would be a year of turnaround for the company as oil and gas production is expected to record a YoY surge of 34% and 38%, respectively.

POL is the least affected by the circular debt

POL is one of the few lucky companies in the energy chain, which is not affected by the ongoing circular debt crisis. Most of POL's oil is supplied to Attock refinery, a group company, which pays POL promptly.

Production from Pindori is sustaining

After touching a low of 74 bopd in April 2009, production from Pindori has increased to a respectable level of 1,750 bopd. This sudden jump in production was due to extensive work over activities. However, the biggest question after this sudden rise in production is regarding its sustainability as total production from Pindori contributes about 12% to POL revenues.

Risks

The major risks associated with POL are fluctuations in oil prices, exchange rate risk as the company's revenues are directly linked to international oil prices denominated in dollars. Furthermore any delays in projects against per our expectations can also pose downside to our forecast.

Financial Highlights

PKR mn	FY09A	FY10A	FY11E	FY12F	FY13F
Revenue	14,047	17,845	21,586	23,620	23,237
Net Profit	5,618	7,437	9,404	10,309	10,310
Shareholder's Equity	25,934	28,276	31,097	34,190	37,283
Total Assets	34,725	37,378	40,004	43,672	46,694
EPS (PKR)	23.75	31.44	39.75	43.58	43.59
DPS (PKR)	18.00	25.50	27.00	29.00	29.00
BVS (PKR)	109.64	119.54	131.46	144.54	157.61
PER x	10.78	8.14	6.44	5.87	5.87
Dividend Yield	7.0%	10.0%	10.5%	11.3%	11.3%
PBV x	2.34	2.14	1.95	1.77	1.62
Net Margin	40.0%	41.7%	43.6%	43.7%	44.4%
ROE (%)	21.7%	27.4%	31.7%	31.6%	28.9%
ROA (%)	16.2%	19.9%	24.3%	24.6%	22.8%

Sources: Annual Reports and AHL estimates

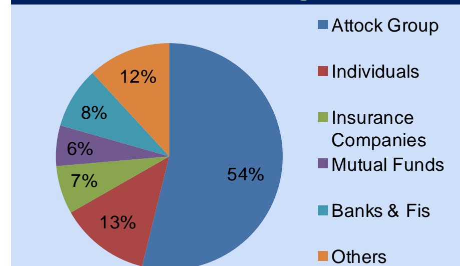
Buy

Target Price (PKR/share)	**317.20**
Last Closing (PKR/share)	**256.02**
Upside	23.9%
KSE Code	POL
Bloomberg Code	POL PA
Reuters Code	PKOL.KA

Key Data

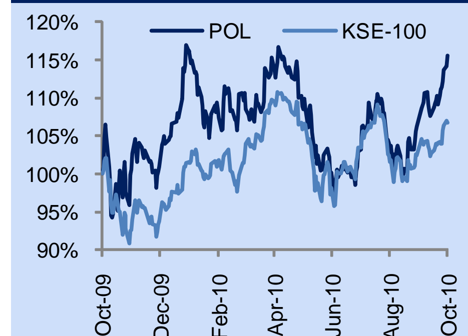
Outstainding Shares (mn)	236.55
Market Cap (US$ mn)	704.19
Market Cap (PKR mn)	60,560.5
Free Float	46%
12M Avg. Daily Turnover	1.75mn
12M High/Low (PKR)	256.02/202.69

Shareholding



Source: Company accounts

Stock Performance



Source: KSE

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Valuation

We have revised our reserved based June'11 target price for POL to PKR 317.2/share. At last closing price of PKR 256.02/share, the stock of POL offers an upside potential of 23.9%, thus we recommend Buy. Our valuation is derived from cost of equity of 20.10%, based on risk free rate of 13.5% and beta of 1.1.

Valuation Summary

FY10 end oil reserves (mn barrels)	87
FY10 end gas reserves (bcf)	2,300
Total Reserves (mnboe)	470
Present value of reserves (PKRmn)	64,349
Exploration Upside	-
Debt	-
Cash & cash equivalents (PKRmn)	7,792
Investment in subsidiary (PKRmn)	2,880
Reserved based value (PKRmn)	75,021
Shares Outstanding (PKRmn)	237
Target Price (PKR/share)	317.2

Source: AHL research

TAL forms the heart of our investment case

Production addition from Tal is the heart of our investment case for POL. The company has 21.1% stake in the TAL Block compared to PPL and OGDC stake of 27.76% each. Due to low equity and production base allows POL to benefit the most. Production from TAL is expected to reach 8,600 bopd and 367 mmcfd of gas in Dec'11 as compared to 3,700 bopd and 190 mmcfd of gas recorded in FY10. This would be mainly on account of additional oil and gas production from Mamikhel and Maramzai.

	Expected production		
TAL Block fields	Oil (bopd)	Gas (mmcfd)	Annualized Impact/EPS-PKR
Manzalai	4,000	290	14.17
Makori	1,290	20	1.54
Mamikhel	2,880	45	3.99
Maramzai	430	12	0.8
Total	8,600	367	20.5

Source:AHL estimates

Production is likely to increase by a 5-year CAGR of 9.4%

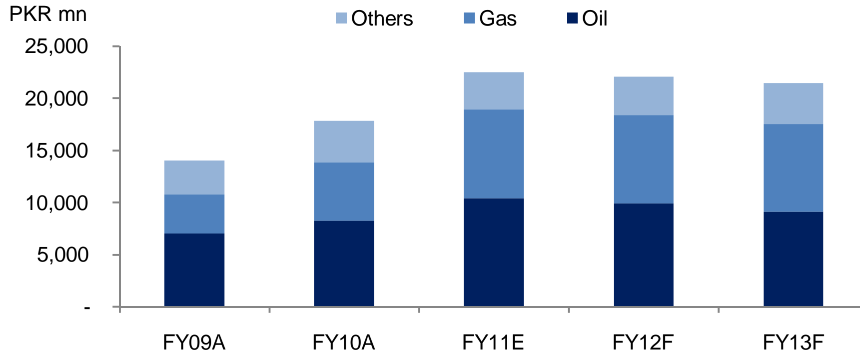
Oil and Gas production of the company is expected to increase at a 5-year CAGR (FY10-FY15) of 9.4% from 5.2mn boe to 7.3mn boe. This rise would mainly to come from TAL block. FY11 would be a year of turn around for the company as oil and gas production is expected to record YoY surge of 34% and 38%, respectively. From FY12 onwards, we believe that the oil and gas production of the company would remain stagnant and hover around 7.1mn boe.

TAL Block will provide stability in earnings

Historically, net earnings of the company were highly sensitive to crude oil prices. This was on account of high weighting (68%) of oil and LPG sales into the revenue mix. Going forward, we expect revenue mix to tilt towards gas as higher gas production from TAL block. In FY11, TAL Block is expected to contribute 71mmcfd

of gas for POL. This would take total gas production of the company at 92mmcfd from 60mmcfd in FY10. In FY15, weightage of oil and LPG is likely to be in the region of 65%.

Revenue Mix



Source: PPIS, AHL Research

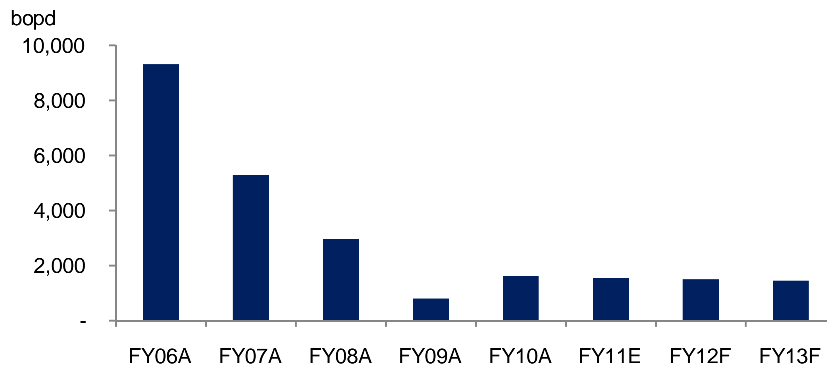
LPG revenue is bringing earnings diversification

In addition to exploration and production, POL also markets Liquefied Petroleum Gas (LPG) produced from its operated fields through its subsidiary Capgas (Pvt) Limited. The company holds a marketing license for LPG under the brand name of POLGAS. Total revenue contribution from LPG stood at 18% in FY10. Going forward, LPG will contribute to diversify revenues for POL, as its contribution will drop to 15% in FY15. This decline in LPG contribution is due to higher share of oil and gas.

Production from Pindori to sustain at 1,500bpd going forward

After touching a low of 74bopd in April 2009, production from Pindori has increased to a respectable level of 1,750 bopd. This sudden jump was due to extensive work over activities. Pindori contributes about 12% to POL revenues, which reflects its significance for the Company. On the conservative side, we have incorporated 1,500bpd of oil from Pindori field going forward.

Pindori Field Oil Production



Source: Company Accounts, AHL Research

Exploratory risk may reduce EPS by PKR 1/share in 1QFY11

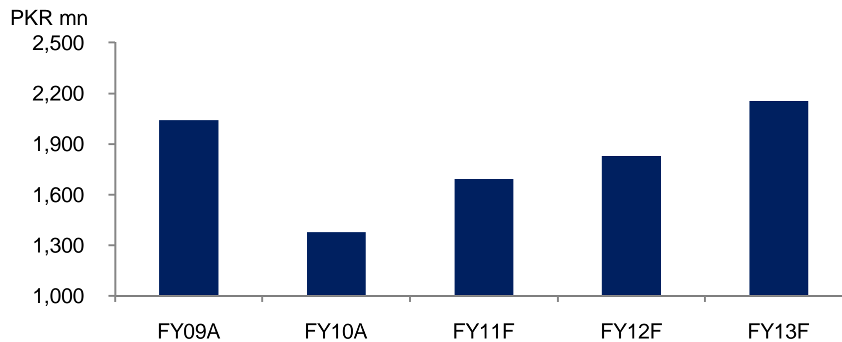
Exploratory well Domial-1 has reached its target depth but currently is under suspension where POL has 19% stake. Therefore, we believe that if this well is declared unsuccessful the company could suffer earnings attrition to the tune of PKR 0.5-1.0/share in FY11.

Dividends from associates will strengthen other income

POL holds 25% stake in National Refinery Limited (NRL), 7% in Attock Petroleum Limited (APL) and 51% in Capgas (Pvt) Limited. POL enjoys healthy dividend income from APL and NRL as both companies have maintained payout ratio of around 45% and 40%, respectively. The Company earned dividend income of PKR 370mn in FY10 (EPS impact of PKR 1.40).

Both APL and NRL have declared a final cash dividend of PKR 15/share and PKR 20/share respectively, along with FY10 results. We expect this would result in an EPS impact of PKR 1.83/share on the company's bottomline. Dividend income is expected to be booked in 2QFY11.

Other Income

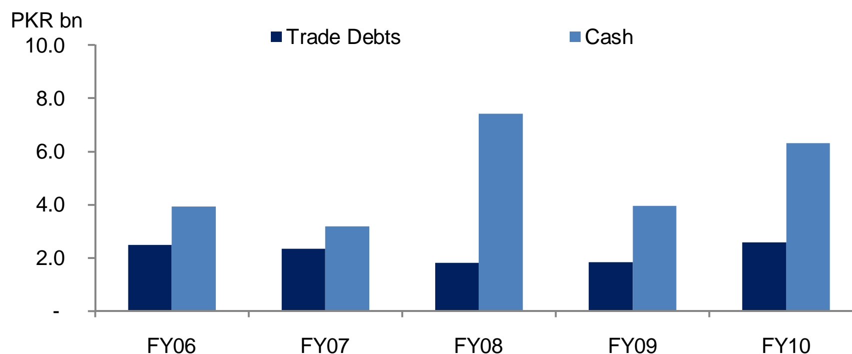


Source: Company Accounts, AHL Research

POL is least affected by the circular debt

POL is one of the few companies in the energy chain which is not affected by the ongoing circular debt crisis. Most of POL's oil is supplied to Attock refinery, a group company which pays POL promptly. Due to minimal gas production, dues from gas distribution are relatively lower. POL is the only company which has shown no significant increase in receivables as compared to OGDCL and PPL.

Trade Debts



Source: Company Accounts

Summary Financials and forecasts, PKR million except per share data and ratios

Income statement	FY09A	FY10A	FY11E	FY12F	FY13F
Net sales	14,047	19,306	21,586	23,620	23,237
Field Expenditures	3,512	4,082	4,965	5,433	5,345
Royalty	1,206	1,596	1,943	2,126	2,091
Exploration Costs	2,058	1,606	1,302	1,397	1,491
Other income	2,042	1,377	1,693	1,829	2,156
Operating profit	3,272	3,630	3,419	4,074	4,661
Profit before taxation	7,185	9,591	12,213	13,389	13,390
Taxation	1,567	2,154	2,809	3,079	3,080
Profit after taxation	5,618	7,437	9,404	10,309	10,310
Earnings per share (PKR)	23.75	31.44	39.75	43.58	43.59
Dividend per share (PKR)	18.00	25.50	28.00	29.00	29.00
Balance sheet	**FY09A**	**FY10A**	**FY11E**	**FY12F**	**FY13F**
Paid-up capital	2,365	2,365	2,365	2,365	2,365
Shareholder's equity	25,934	28,276	31,097	34,190	37,283
Non current liabilities	6,021	4,927	5,353	5,531	5,424
Current Liabalities	2,769	4,175	3,553	3,952	3,987
Total Liabalities	8,790	9,102	8,907	9,483	9,411
Non current assets	24,925	25,672	26,299	27,207	27,980
Current assets	9,799	11,706	13,705	16,465	18,714
Total assets	34,725	37,378	40,004	43,672	46,694
Cash flows	**FY09A**	**FY10A**	**FY11E**	**FY12F**	**FY13F**
Net operating cash flow	5,489	9,959	10,689	11,943	12,558
Net investing cash flow	(4,333)	(2,308)	(2,510)	(2,966)	(2,850)
Net financing cash flow	(5,034)	(6,401)	(5,956)	(6,957)	(7,324)
Net change in cash	(3,877)	1,250	2,222	2,020	2,385
Cash at the end of the period	3,946	5,195	7,418	9,438	11,823
Ratios	**FY09A**	**FY10A**	**FY11E**	**FY12F**	**FY13F**
Dividend yield	7.0%	10.0%	10.9%	11.3%	11.3%
Return on average equity (ROE)	21.7%	26.3%	30.2%	30.2%	27.7%
Return on assets (ROA)	16.2%	19.9%	23.5%	23.6%	22.1%
Price to earning ratio (PER)	10.78	8.14	6.44	5.87	5.87
Book value per share (PKR)	109.64	119.54	131.46	144.54	157.61
Price to book ratio (PBR)	2.34	2.14	1.95	1.77	1.62
Net profit margin	40.0%	38.5%	43.6%	43.6%	44.4%

ARIF HABIB LIMITED

Company Report

November 11, 2010

Pakistan Petroleum Limited — Oil and Gas

Sizeable upside potential

At the current price level, the stock of PPL is offering an upside potential of 22.5% based on our June'11 reserved based target price of PKR 235.3/share. In addition to this the scrip offers a dividend yield of 7.8% based on our FY11E earnings estimates. Furthermore, the stock is currently trading at a FY11E P/E of 7.0x based on our Jun'11 earnings of PKR 27.52/share.

Production driving earnings growth

Net earnings of the company are expected to record a staggering rise of 41% YoY in FY11 to PKR 32.8mn (EPS: PKR 27.52). This is on account of rise in oil and gas production of 49% YoY and 6% YoY to 8,200bopd oil and 990mmcfd, respectively.

Sensitivity to oil price is increasing

Oil driven revenue is expected to increase from the current 13% to 19% in FY11. From FY11 onwards, oil contribution in total revenue would marginally increase by 1% and hover around 20%-22% till FY15.

PPL likely to be the beneficiary of TGR

PPL stands to benefit from government's growing focus on Tight Gas Reserves (TGR) as it holds major stake in largest gas based fields like Sawan (PPL 26% stake) and Miano (PPL15% stake), which have huge TGR potential.

Mounting receivables are not going to hurt PPL

Despite mounting trade receivables PPL cash position is improving. As of FY10 PPL's has cash balance of PKR1.9bn compared to 1.3bn in FY09 and PKR260mn in FY05. Moreover, the company's short term investments have doubled in one year to PKR 27bn from PKR 13bn witnessed as of June 30, 2009.

Risks

The major risks associated with PPL are delay in commencement of production from Maramzai and Mela against our expected timeline, fluctuations in oil prices and exchange rate risk as the company's revenues are directly linked to international oil prices denominated in dollars.

Financial highlights

PKR mn	FY09A	FY10A	FY11E	FY12F	FY13F
Revenues	61,580	59,962	77,163	85,080	92,413
Net profit	27,703	23,321	32,863	36,232	39,256
Shareholders' Equity	63,059	79,906	95,968	113,090	132,025
Total Assets	82,916	107,580	125,927	145,416	167,079
EPS (PKR)	23.20	19.53	27.52	30.32	32.85
DPS (PKR)	13.00	9.00	15.00	16.00	18.00
BVS (PKR)	52.81	66.92	80.38	94.64	110.48
PER x	8.3	9.8	7.0	6.3	5.8
Dividend Yield	6.8%	4.7%	7.8%	8.3%	9.4%
PBV x	3.6	2.9	2.4	2.0	1.7
Net Margin	45.0%	38.9%	42.6%	42.6%	42.5%
ROA	38.5%	24.5%	28.1%	26.7%	25.1%
ROE	51.9%	32.6%	37.4%	34.7%	32.0%

Source: Company accounts, AHL estimates

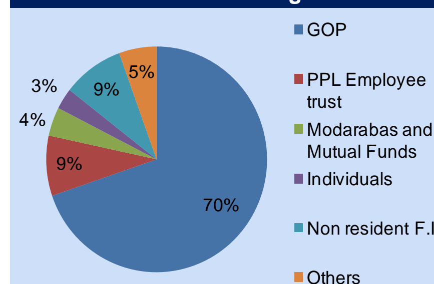
Buy

Target Price (PKR/share)	**235.30**
Last Closing (PKR/share)	**192.01**
Upside	22.5%
KSE Code	PPL
Bloomberg Code	PPL PA
Reuters Code	PPL.KA

Key Data

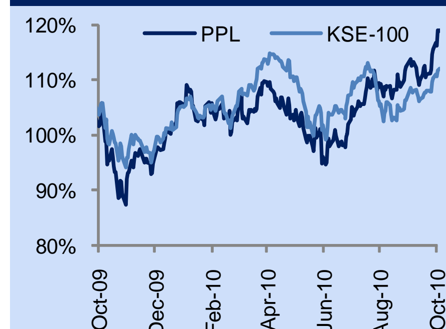
Outstainding Shares (mn)	1,194.98
Market Cap (US$ mn)	2,668.00
Market Cap (PKR mn)	229,447.8
Free Float	21%
12M Avg. Daily Turnover	1.51mn
12M High/Low (PKR)	192.01/136.25

Shareholding



Source: Company accounts

Stock Performance



Source: KSE

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Valuation

We have revised our reserved based June'11 target price for PPL to PKR 235.3/share. At last closing price of PKR 192.01/share, the stock of PPL offers an upside potential of 22.5%, thus we recommend Buy. Our valuation is derived from cost of equity of 19.8%, based on risk free rate of 13.5% and beta of 1.1.

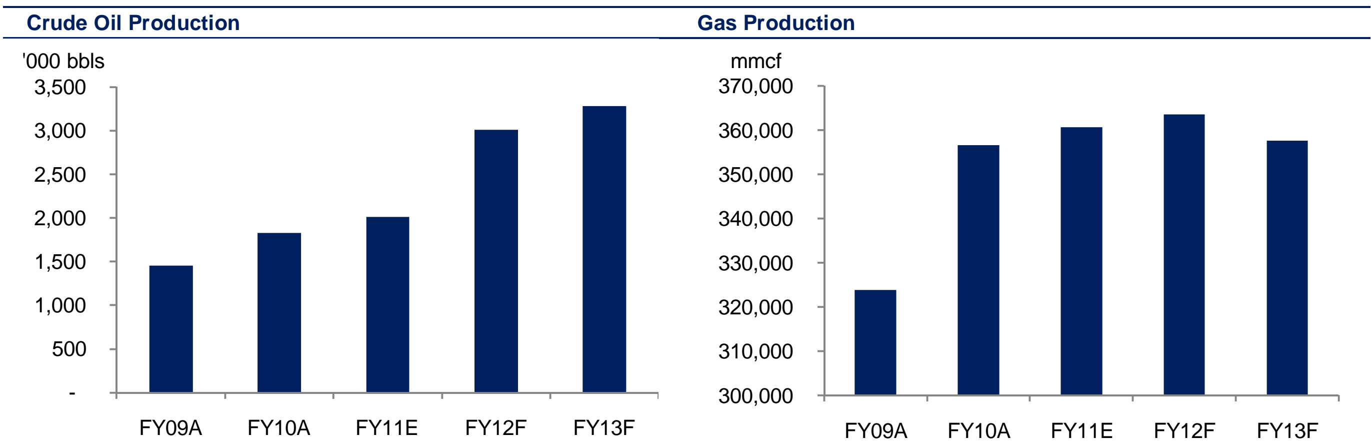
Valuation Summary

FY10 end oil reserves (mn barrels)	97
FY10 end gas reserves (bcf)	10,214
Total Reserves (mnboe)	1,799
Present value of reserves (PKRmn)	
Exploration Upside	251,747
Debt	-
Cash & cash equivalents (PKRmn)	-
Investment in subsidiary (PKRmn)	29,169
Reserved based value (PKRmn)	280,916
Shares Outstanding (PKRmn)	1,194
Target Price (PKR/share)	235.3

Source: AHL research

Production driving earnings growth

Net earnings of the company are expected to record a staggering rise of 41% YoY in FY11 to PKR 32.8mn (EPS: PKR27.52). This is on account of rise in oil and gas production by 49% YoY and 6% YoY to 8,200bopd and 990mmcfd, respectively. This rise is mainly on account of annualized production impact from Nashpha, Latif and Mamikhel fields which came online in 4QFY10. Moreover, expected commencement of production from Mela 03 and Maramzai by 2QFY11 will further contribute to this rise. Mela-03 is expected to contribute 3,000 bopd while enhancement of production from Mamikhel would be around 600 bopd.



Source: Company Accounts, AHL Research

Source: Company Accounts, AHL Research

PPL's earning sensitivity for oil is on the rise

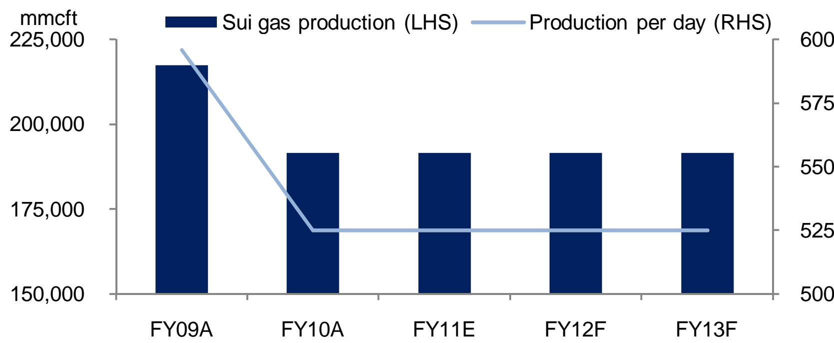
Around 88% of the company's revenue in FY10 was driven by gas. However, with commencement of production from Tal Block, Mela and Naspha, oil contribution to revenue is expected to rise from 12% in FY10 to 19% in FY11. Beyond FY11

onwards, oil share in the total revenue would increase marginally by 1% and hover around 20%-22% till FY15.

Depleting Sui Reserve not a worrisome factor

Fulfilling the gas needs of the country since 1952, Sui, is exhibiting signs of depletion. Production from this field has declined to 562mmcfd in FY2010 as compared to 667mmcfd in FY2006, dropping at an average rate of 5% for the last 4 years. Current contribution of Sui is 60% to the total gas production of the company. However, this decline will not much affect the earnings of the company as this will be largely mitigated by the new discoveries (Manzalai, Mamikhel, Gambit and Latif) besides; the company is also drilling in Sui-88 and Sui-92 to offset the impact of decline in production from other wells. Sui field is projected to decline by an average of 4% over the next four years to 475mmcfd.

Sui Field Production



Source: Company Accounts, AHL Research

News on exploration front

As a result of extensive exploration activities four new discoveries were made during the year in partner operated blocks (Naspha, Maramzai, Rehman and Latif North). Currently on the exploration front, Tolanj in the TAL block is being drilled which is expected to reach completion by Dec'10 where PPL stake is 27.8%. The potential from this exploration is high considering TAL blocks discoveries in the past.

PPL likely to be the beneficiary of TGR

PPL stands to benefit from government's growing focus on Tight Gas Reserves (TGR) as it holds major stake in largest gas based fields like Sawan (PPL 26% stake) and Miano (PPL15% stake), which have huge TGR potential. The policy on TGR is yet to be finalized. However, potential benefits from TGR would provide an upside to PPL's earnings. Further the company is also likely to benefit from its joint venture operation with foreign companies (eights fields out of total seventeen are operated by foreign partners), as they would be able to provide technical expertise in order to extract TGR.

PPL is going global

PPL has started to spread its exploring tentacles beyond boarders as the Company is actively pursuing exploration activities in five countries, namely Yemen, Iraq, Iran, Algeria, and Senegal. The Company was successful in getting the exploration award of Block-29 in Yemen, where PPL has 50% non-operating stake with OMV. In Iraq, the Company has pre-qualified to participate in second bidding round for field development. PPL has also prequalified in Iran to participate in exploration

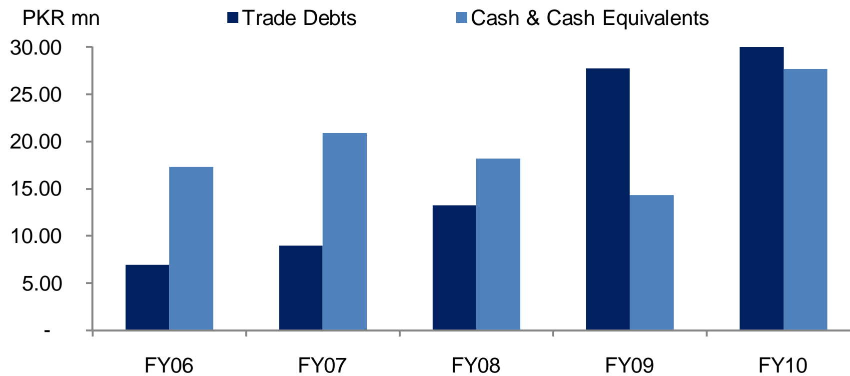
activities and evaluation of two blocks is underway. Technical evaluation of a block in Senegal has been completed. Realization of these activities is likely to bear fruits for the Company in two to three years down the road.

Mounting receivables are not going to hurt PPL

According to the FY10 financial statements, trade debts of the company were recorded at PKR 31bn, exhibited a rise of 11% in contrast to same period last year. Sui Northern Gas Pipeline Ltd (SNGPL) remained the major debtor with PKR 13.65 billion (FY09: PKR 13.59 billion) followed by Sui Southern Gas Company Ltd (SSGC) of PKR 7.62 billion (FY09: PKR 8.75 billion), Water and Power Development Authority PKR 7.23 billion (FY2009: PKR 3.48 billion) and Attock Refinery Ltd (ARL) PKR 1.52bn (FY09: PKR 1.80 bn). This is due to prevailing circular debt situation, driven mainly by the power sector. However, if we compare trade debts of OGDCL of PKR 86bn, PPL receivables' do not seem a big amount but it is higher than POL trade debts of PKR 2.5bn. Despite mounting trade receivables PPL cash position is improving. As of FY10 PPL's has cash balance of PKR 1.9bn compared to 1.3bn in FY09 and PKR 260mn in FY05. Moreover, the company's short term investments have doubled in one year to PKR 27bn from PKR 13bn witnessed as of June 30, 2009.

Going forward, we expect the intensity of the circular debt to hover around the same level as witnessed in FY10. However, due to PPL's healthy free cash flow position and strong balance sheet, the risk of dwindling payout is low. Based on our FY11 and FY12 dividend payout estimates, the stock of PPL is offering an attractive dividend yield of 7.8% and 8.6% respectively.

Trade debts and Liquid Assets



Sources: Company Accounts, AHL Research

Summary Financials and forecasts, PKR million except per share data and ratios

Income statement	FY09A	FY10A	FY11E	FY12F	FY13F
Net sales	61,580	59,962	77,163	85,080	92,413
Field Expenditures	13,161	18,273	16,226	17,815	19,451
Royalty	7,463	7,076	9,645	10,635	11,552
Other income	4,150	2,638	1,505	1,580	1,660
Operating profit	3,272	3,630	3,419	4,074	4,661
Profit before taxation	41,908	34,258	49,049	54,078	58,591
Taxation	14,206	11,208	16,186	17,846	19,335
Profit after taxation	27,703	23,321	32,863	36,232	39,256
Earnings per share (PKR)	23.20	19.53	27.52	30.35	32.88
Dividend per share (PKR)	13.00	9.00	15.00	16.00	18.00
Balance sheet	**FY09A**	**FY10A**	**FY11E**	**FY12F**	**FY13F**
Paid-up capital	8,299	9,958	11,950	11,950	11,950
Shareholder's equity	63,059	79,906	94,859	112,816	113,090
Non current liabilities	5,209	8,050	9,258	10,184	11,202
Current Liabalities	14,648	19,623	20,710	22,609	24,363
Total Liabalities	19,858	27,673	29,968	32,793	35,565
Non current assets	37,477	44,522	51,526	60,933	72,386
Current assets	45,439	63,057	74,401	84,483	94,693
Total assets	82,916	107,580	125,927	145,416	167,079
Cash flows	**FY09A**	**FY10A**	**FY11E**	**FY12F**	**FY13F**
Net operating cash flow	13,293	26,460	25,957	37,884	40,800
Net investing cash flow	(8,770)	(6,513)	(4,795)	(5,097)	(5,225)
Net financing cash flow	(8,354)	(6,613)	(17,910)	(19,104)	(21,492)
Net change in cash	(3,830)	13,334	3,252	13,683	14,083
Cash at the end of the period	1,384	14,719	17,970	32,132	46,215
Ratios	**FY09A**	**FY10A**	**FY11E**	**FY12F**	**FY13F**
Dividend yield	6.8%	4.7%	7.8%	8.6%	9.7%
Return on average equity (ROE)	43.9%	29.2%	34.6%	32.1%	30.1%
Return on assets (ROA)	33.4%	21.7%	26.1%	24.9%	23.5%
Price to earning ratio (PER)	8.28	9.83	6.98	6.14	5.67
Book value per share (PKR)	75.99	80.24	95.26	94.41	94.64
Price to book ratio (PBR)	2.53	2.39	2.02	2.39	2.03
Net profit margin	45.0%	38.9%	42.6%	42.6%	42.5%

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