Momentum of inventory gains continue in 2QFY22

NEXT CAPITAL

Oil Marketing Companies — Overweight

February 4, 2022

Pakistan Equities
Oil Marketing Companies

Key Points

- According to provisional volumetric figures published by OCAC, total sales of POL items stood at 5.25mn tons during 2QFY22 depicting a modest growth of 4.8%YoY.
- HSD sales outperformed considerably by posting 8% growth on both YoY and QoQ comparisons to stand at 2.26mn tons.
- Our coverage universe has done extremely well with all companies improving their market shares relative to SPLY.
- In spite of ex-refinery prices drifting down 14% for MS and 11% for HSD during Dec'21, the quantum of increase and the higher monthly sales during preceding Oct-Nov'21 would be adequate to ensure PSO/APL/SHEL/HTL to post inventory gains of approx. PKR6.45/1.36/1.28/0.01bn, respectively (pre-tax)
- Next OMC Universe is expected to post bottom-line of PKR14.3bn, a staggering increase of 120%YoY. Primary reasons are a higher quantum of inventory gains and increased retail market share. This growth is supported by PSO, APL and HTL, which are expected to post earnings growth of 168%, 179% and 15%, respectively.
- We anticipate our entire coverage universe to announce payouts. Our top picks in the OMC sector are PSO and HTL

Seasonally low FO offtakes weigh down on volumetric growth; HSD sales, however, outperform

According to provisional volumetric figures published by OCAC, total sales of POL items stood at 5.25mn tons during 2QFY22 depicting a modest growth of 4.8% on YoY basis. However, on a sequential basis, POL sales suffered a substantial dip of 10.5%, primarily attributable to slowdown in FO offtakes by power sector (FO offtakes during 2QFY22 stood at 0.63mn tons versus 1.27mn tons during previous quarter). Winter season usually witness a slowdown in FO sales, but the quarter under review suffered the brunt of higher average local prices too (increasing substantially from PKR104,000/ton in 1QFY22 to approx. PKR130,000/ton), further weighing down on already waning demand outlook. Despite some supply-chain issues still persisting with RLNG procurement, FO inventory kept piling up at storages of refineries and even led to shutdowns. On the other hand, HSD sales outperformed considerably by posting 8% growth on both yearly and quarterly comparison to stand at 2.26mntons. We believe strong performance of agricultural sector during Kharif harvesting and Rabi sowing season, as well as increasing mix of documented sales in total sales are the biggest reasons for this sustained momentum in HSD sales.

Listed space was able to increase their retail market share

The increasing proportion of significant retail fuels (MS, HOBC and HSD) in overall sales mix contributes positively to cash-based earnings, hence the prospect of improving (or at the very least) retaining their market share becomes extremely important to recurring earnings. In this regard, our coverage universe has done extremely well with all companies improving their market share relative to SPLY. PSO's retail market share jumped up to 46.5% during 2QFY22, a significant improvement from 43.8% of 2QFY21. APL, in recent times, has been performing admirably as evident from its growing market share of 8.5% (7.98% in previous quarter and 7.24% in SPLY). SHEL and HTL have also increased their market shares by 0.43 and 0.05ppts (low base), respectively on yearly comparison.

Another quarter of phenomenal inventory gains

The consistent bi-monthly increase in local ex-refinery prices during Oct-Nov'21 will ensure another quarter of phenomenal inventory gains for our coverage universe. It's important to reiterate that in spite of ex-refinery prices drifting down 14% for MS and 11% for HSD during Dec'21, the quantum of increase and the higher monthly sales during preceding Oct-Nov'21 would be adequate to ensure PSO/APL/SHEL/HTL to post inventory gains of approx. PKR6.45/1.36/1.28/0.01bn, respectively (pre-tax). Although, we expect the significant decline in Dec'21 ex-refinery prices would lead to lower inventory gains when compared with 1QFY22, which is also evident from the decline in sequential GMs (our expectations of GMs during 2QFY22 stand at 3.83%/4.61%/7.48%/20.4% for PSO/APL/SHEL/HTL).

SHEL would be the biggest beneficiary of lower exchange losses

In our coverage universe, SHEL is the most exposed to volatility in exchange rates and since 2QFY22 witnessed local currency depreciation at a lower magnitude than previous quarter (currency devaluation of 4.3% in 2Q versus 8.2% in 1Q), we expect SHEL to record exchange losses worth PKR1.5bn (down from PKR2.35bn in previous quarter). As a result, SHEL would potentially post QoQ earnings growth of 59%, but would however, decline by a massive 62% on YoY comparison (4QCY20 witnessed currency appreciation,

Key Data

Mkt. Cap. (USDmn)	1,108
Mkt. Cap. (PKRbn)	194.5
Index Weightage (KSE-100)	3.3%
Number of Listed Companies	7

Source: PSX, Next Research

EPS estimates

	2QFY22E	YoY%	QoQ	1HFY22E	YoY%
PSO	25.02	168	-2%	50.56	149
APL	18.55	179	-23%	42.55	97
SHEL*	2.21	-62	59%	13.66	N/A
HTL	1.78	15	138	2.53	16

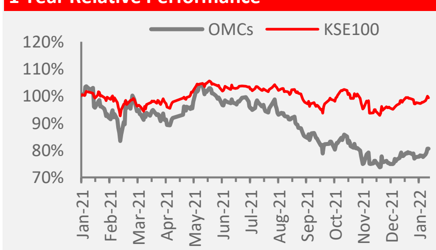
SHEL 4QCY21E; CY21E
Source: Company Accounts, Next Research

DPS estimates

	2QFY22E	1HFY22E
PSO	8.00	8.00
APL	17.50	17.50
SHEL*	6.00	6.00
HTL	2.00	2.00

*SHEL 4QCY21E; CY21E
Source: Company Accounts, Next Research

1 Year Relative Performance



Source: PSX, Next Research

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hence, proving extremely beneficial for SHEL). This phenomenon is completely opposite for PSO and APL, whom have undergone massive yearly earnings growth of 168% and 179%, but declining on sequential comparison.

Dividend payouts, everywhere!

Next OMC Universe is expected to post bottom-line of PKR14.3bn, a staggering increase of 120% on yearly comparison. Primary reasons are a higher quantum of inventory gains and increased retail market share. This growth is supported by PSO, APL and HTL which are expected to post earnings growth of 168%, 179% and 15% respectively. Although, this profitability would clock-in marginally below 1QFY22 profitability of PKR14.8bn. But in-spite of sequential lower profitability, cumulative earnings have been outstanding and we expect our entire coverage universe to provide investors with a dividend payout. We expect PSO to receive a sizable penal income from its creditors considering second tranche payment to IPPs during Dec'21. We estimate DPS of PKR8.00 by PSO. APL, on the other hand is almost unscathed from any circular debt issue and we expect it to announce a cash payout of PKR17.50/share. HTL would continue its history of semi-annual dividends with a payout of PKR2.00/share, but perhaps, the biggest surprise could come from SHEL considering its return to full-year profitability after a period of 3 years. We anticipate SHEL to surprise investors with a cash payout of PKR6.00/share.

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Rating	Sector's proposed weight in the portfolio
Over Weight	> Weight in KSE 100 index
Market Weight	= Weight in KSE 100 Index
Under Weight	< Weight in KSE 100 Index

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Rating	Expected Total Return
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Neutral	$0\% \geq R < 15\%$
Sell	$R < 0\%$

Where;

R = Expected Dividend Yield + Expected Capital Gain

R' is before tax

Investment horizon is between six months to twelve months

Ratings are updated regularly based on the latest developments in the economy/sector/company, changes in stock prices, and changes in analyst's assumptions.

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