



Oil & Gas Marketing Sector



APL: EXPANDING STAR

June 2010

PAKISTAN RESEARCH
OMC Sector

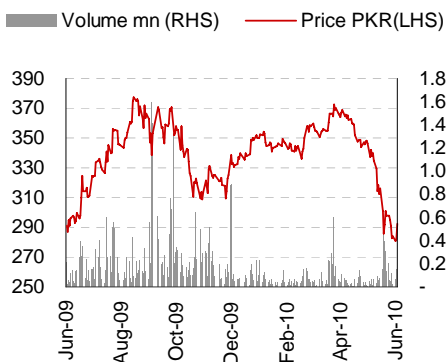
BUY

Fair Value: PKR 545

Current Price: PKR 293

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Price and Volume Graph



APL: EXPANDING STAR
INVESTMENT SUMMARY

- **Expanding market share:** Attock Petroleum Limited (APL) is the 4th largest Oil Marketing Company (OMC) in Pakistan. During the last 3 years APL has increased its number of retail outlets with CAGR of ~18% and now operates 246 retail outlets. In terms of volumetric sales, APL accounts for 7.0% of total market share and has witnessed rapid volumetric growth in sales during FY09 of around 33% and 37% for Motor Spirit (MS) and High Speed Diesel (HSD) respectively, compared to industry average of 7% and -6% respectively.
- **Market leader in Asphalt:** Currently APL is the only OMC which markets Asphalt and hence it holds significant monopoly in the market. Asphalt sales volume has experienced 4year CAGR of ~3% and contributes ~50% towards APL's total gross profit. APL has significant synergies with the Asphalt producing refineries associated with Attock Group of Companies and hence places it in an even more attractive position.
- **Relative hedge from circular debt:** Being a non-government entity, APL chose to keep itself away from circular debt menace. APL had to pay the cost for this choice by losing market share by 137bps (from 7.3% in FY07 to 6.0% during FY09) in furnace oil (FO) segment. However benefits obtained were prevention of rising financial charges and increased concentration on retail network expansion. Nonetheless, as circular debt issue eases off, APL can benefit by regaining its market share in the segment, thus providing upside risks to our future volumetric projections.
- **Synergies from the group:** APL is an associated member of Attock Group of Companies, the only vertically integrated group in the field of oil and gas sector of Pakistan. With two strategically located refineries: Attock Refinery Limited (ATRL) in the north and National Refinery Limited (NRL) in the south of the country APL can 1) ensure smooth product supply 2) reap pricing benefits in the export market and 3) take advantage of its associated refineries through high commission and handling incomes.
- **Outlook:** We expect modest CAGR of around 2% in volumetric offtakes of Asphalt to continue as domestic economy gets back on track. APL should benefit from resolution of circular debt issue and experience 5% growth in sales volume of FO during FY11. We expect sales volumes of MoGas for APL to cross 100,000 MT mark by FY11 due to 1) persistence in power outages, 2) continued growth in transport sector and 3) expansion in its retail network.
- **Compelling valuations:** At yesterday's closing price of PKR293/share, APL currently offers an upside potential of 86% to our DCF-based fair value of PKR545/share. APL is attractively valued with FY11E PER of 4.7x. We recommend a BUY stance on the stock.

Financials

	FY09A	FY10E	FY11E
EPS(PKR)	53.5	55.3	62.4
Price to Earnings (x)	5.5x	5.3x	4.7x
Dividend Yield (%)	9.7%	11.5%	13.0%
EPS Growth (%)	16.6%	3.3%	12.9%
Return on Equity (%)	43.5%	38.2%	36.9%
Return on Assets (%)	16.9%	16.3%	15.3%

Source: BMA Research

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INVESTMENT RATIONALE

Expansion Plans: Well fueled growth

Attock Petroleum Limited (APL) is the 4th largest Oil Marketing Company (OMC) in Pakistan. APL since inception has adopted an aggressive expansion strategy. During the last 3 years APL has increased its number of retail outlets from 177 as at Jun07 to 246 as at Jun09, registering CAGR of ~18%. APL now operates 3.9% of total OMC retail outlets in Pakistan and in terms of volumetric sales accounts for 7.0% of total market share. It has witnessed rapid volumetric growth in sales during FY09 of around 33% and 37% for Motor Spirit (MS) and High Speed Diesel (HSD) respectively, compared to respective industry averages of 7% and -6%.

For the next 5 year period, we expect APL to experience CAGR of 8.8% and 2.8% in its top and bottom line; supported by 1) its aggressive expansion strategy with respect to retail network 2) ~40% of APL's total assets being liquid in nature and 3) recently shown interest to acquire Admore Gas Pvt. Ltd.

Asphalt: Largest slice of the cake

Currently APL is the only OMC which markets Asphalt and hence APL holds significant monopoly in the market. Asphalt is only produced by APL's associated refineries: National Refinery Limited (NRL) and Attock Refinery Limited (ATRL), thus providing the company with significant synergies with the group. Asphalt sales volume has experienced 4year CAGR of ~3% and contributes ~50% towards APL's total gross profit.

Backed by high margins and 100% market share in the OMC sphere, exposure to asphalt makes APL one of the most attractively positioned company in the sector.

Circular Debt: Weighing the odds

Being a private sector entity, APL managed to keep itself away from circular debt menace. Circular debt has taken toll on entire value chain, resulting in acute liquidity shortages. PSO, the primary burden holder of circular debt is facing soaring financial charges which increased by 7.5x since FY07. APL had to pay the cost for this choice in the form of lost sales in Furnace Oil (FO) segment which contributed 20% towards APL's total gross profit during FY09. The company lost market share by 137bps, from 7.32% in FY07 to 5.95% during FY09. In terms of FO sales volume, APL witnessed 12.30% decline over FY07-09 period.

However, benefits outweigh costs as APL was able to 1) prevent rising financial charges 2) maintain liquidity and collection ratios 3) increase concentration on retail network expansion and higher volumetric sales of high margin products. Nonetheless, as circular debt issue eases off, APL can benefit by regaining its market share in FO sales, thus providing upside risk to future volumetric projections.

Attock Group: Value through synergies

APL is an associated member of Attock Group of Companies, the only vertically integrated group in oil and gas sector of Pakistan. APL possesses high synergies with its parent group and therefore is well positioned as far as

petroleum products supplies are concerned. With two strategically located refineries: ATRL in the north and NRL in the south of the country, APL can 1) ensure smooth product availability for its customers, 2) reap benefits of pricing benefits in the export market and 3) take advantage of its associated refineries through high commission and handling incomes.

Valuations: Potential upside of 86%!

Using a risk-free rate of 12.5% and equity risk premium of 6%, our DCF-based fair value for APL stands at PKR545/share.

At yesterday's closing price of PKR293/share, APL currently offers an upside potential of 86% to our DCF-based fair value of PKR545/share. APL is attractively valued with FY11E PER of 4.7x. We recommend a BUY stance on the stock.

Regional Comparison: Attractively positioned

APL currently trades at FY11E PER of 4.38x while the regional median FY11E PER is 8.56x, reflecting 49% discount to its peers. Additionally, the stock is also trading at 73% discount to the regional peers' FY11E EV/EBITDA average of 5.56x. APL has YTD beta close to that of its regional peers, while its dividend yield is being reflected at 7.85% compared to regional peers' average of 6.15%.

The regional oil companies represent a useful benchmark for the local market, however it should be noted that most of these companies are integrated oil and gas companies having both refinery and marketing operations (midstream and downstream). Refineries globally are trading cheap due to concerns emanating from abysmal GRMs, therefore most of APL's peers (mentioned in the table below) already reflect substantial discount to their respective markets. APL however is structurally different from its regional peers with its operations only limited to oil marketing; yet it is currently trading at FY11E PER of 4.38x compared to regional peer average of 8.56x, which makes it even more attractive. Shell Oman is the only comparable regional company which is also a purely oil marketing concern and for which estimates are readily available. Compared to Shell Oman, APL is even cheaper as Shell Oman is trading above regional oil companies' average.

Company	Country	Ticker	Market Cap	Beta	PER (x)			EV/EBITDA (x)		P/B	P/S	Dividend Yield
					YTD	FY10E	FY11E	FY10E	FY11E			
		Bloomberg	USD mn									
Pakistan State Oil	Pakistan	PSO PK	45,880	1.07	4.56	4.26	2.25	2.64	1.65	0.07	2.34%	
Shell Pakistan	Pakistan	SHEL PK	16,060	0.88	NA	8.51	NA	4.41	2.33	NA	11.99%	
Attock Petroleum	Pakistan	APL PK	16,700	0.92	5.47	4.38	NA	1.50	2.38	0.27	7.85%	
Caltex Australia Limited	Australia	CTX AU	3,020	1.14	9.59	10.54	NA	5.26	1.03	0.17	2.69%	
Hindustan Petroleum Corp	India	HPCL IN	116,710	0.55	8.13	8.02	7.63	7.85	1.03	0.11	1.95%	
Petronas Dagangan BHD	Malaysia	PETD MA	9,080	0.72	12.06	11.31	NA	6.04	1.99	0.44	4.97%	
Petron Corp	Philippines	PCOR PH	62,810	0.45	NA	12.18	NA	8.74	1.60	NA	NA	
Bangchak Petroleum PCL	Thailand	BCP TH	16,030	0.74	2.34	4.90	4.61	4.24	0.60	0.13	11.54%	
Shell Oman Marketing	Oman	SOMS OM	187	0.33	13.67	12.90	9.70	9.35	9.41	0.61	5.88%	
Regional Average				0.76	7.97	8.56	6.04	5.56	2.45	0.26	6.15%	

Upside to our valuations: Admore adding more

APL has recently shown interest in acquiring Admore Gas (Pvt) Ltd. We envisage the merger to have a positive impact, however changes cannot be incorporated until further details are obtained post due diligence process. These affects will all be positive on APL's balance sheet and operating performance. Acquisition of Admore, for instance, can provide 159% jump in number of retail outlets, allowing APL to benefit from increased volumetric sales. In this manner APL can utilize its excess cash and generate post-acquisition ROE which is likely to be much higher than the return currently made on its excess liquidity.

Potential Risk Factors

Persistence in inter-corporate circular debt

We expect industry FO sales to grow by 5% during FY11 due to rising energy requirements of the country and increased reliance on thermal energy sources. However, persistence in circular debt issue can continue to discourage APL to regain market share in FO.

Change in POL pricing formula or reduction in marketing margins

One of the key risks to valuations is any reduction in distributor margins (% on product price) or lowering of absolute cap margins imposed by OGRA (currently set at USD80/bbl). APL however is far less sensitive to regulated margins compared to its peers (currently regulated products contribute 47% towards APL's gross profit). On the other hand, deregulation of product prices may provide upside risks for the stock.

Threat of new entrants

GoP has recently relaxed capital requirements for new entrants in OMC sector, from PKR6bn to PKR0.1bn, thus increasing the possibility of more competitors entering the industry and saturating the expanding market.

Lower than expected future Asphalt sales

Asphalt being a deregulated product, generates high margins for APL and contributes ~50% towards its total gross profit. Lower than expected future Asphalt sales will directly and significantly affect APL's top and bottom line.

Abnormal decline in oil prices

If international oil prices undergo a major correction, the company would be adversely affected by 1) minor inventory losses and 2) decline in absolute margins on its products. For our valuations, we have assumed a stable oil price of USD75/bbl going forward.

Non availability of lucrative sites

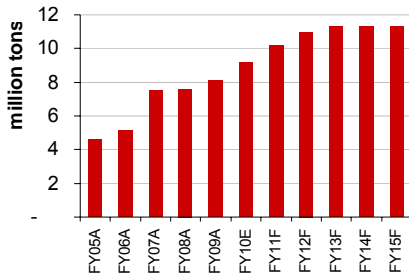
The company's expansion plans might be stalled due to non availability of lucrative sites for retail stations, particularly in urban and highly populated areas where sales per pump are much higher.

INDUSTRY DYNAMICS

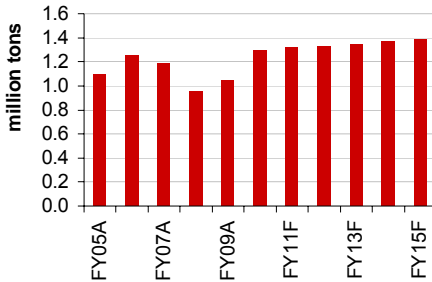
Demand for petroleum (POL) products

The Oil Marketing industry has experienced average CAGR of 5.1% in total sales volume over last 5 year period. Furnace Oil (FO), High Speed Diesel (HSD), Motor Spirit (MS), Jet fuel (JP) and Asphalt are major selling petroleum products, with share in total sales of 42.5%, 40.3%, 8.0%, 5.5% and 1.5% respectively.

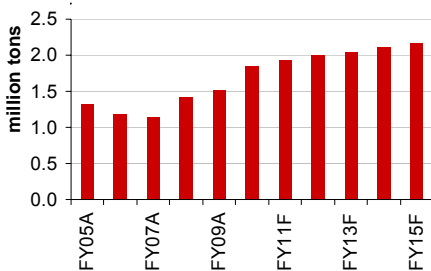
Industry - FO sales volume



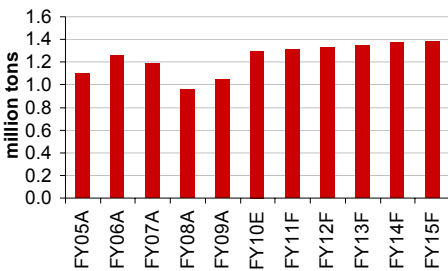
Industry - JP sales volume



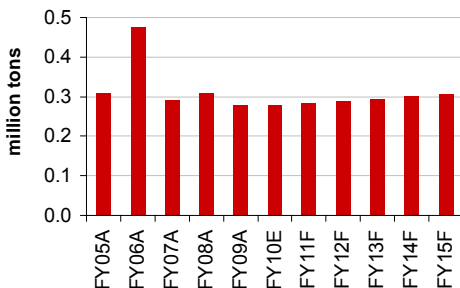
Industry - MS sales volume



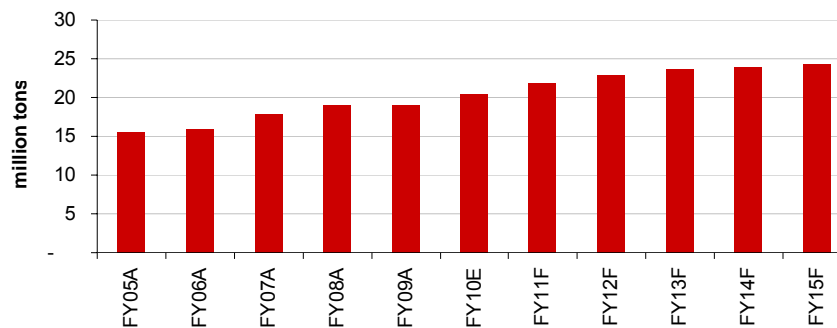
Industry - JP sales volume



Industry - Asphalt sales volume



Industry's total POL sales volume



Source: OCAC, BMA Research

FO sales experienced staggering CAGR of 16.4% in sales volume over last 5 year period, primarily due to increased reliance of power sector on thermal energy and growth in energy requirements of the country. We expect FO volumetric sales to experience CAGR of 4.3% over next 5 year period.

HSD sales volume on average remained flat over the last 5 years, on the back of subsidy elimination on the product. We expect HSD sales volume to experience CAGR of 1% going forward on account of growth in transport sector and increased power outages encouraging HSD usage for private generators.

MS sales have experienced CAGR of 4.3% in sales volume over last 5 year period, due to 1) growth in transport sector 2) reduced price differential between MS and CNG and high convenience yield attached to MS 3) increased power outages. We expect MS sales volume to experience CAGR of 3.0% going forward.

JP's volumetric sales also remained flat over the last 5 year period. Growth in exports have been offsetting fall in domestic sales. We expect JP sales volume to experience meager CAGR of 0.8% going forward.

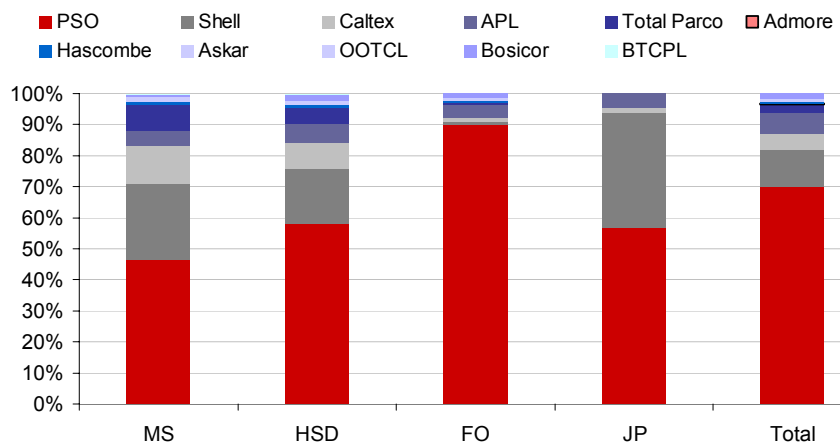
Asphalt sales are dependent on road construction activity which in turn is driven by various factors discussed in the next section. It experienced CAGR of 2.8% in sales volume over last 5 year period while we expect CAGR to remain in the vicinity of 2.0% going forward.

Major players in the market

PSO is the major and most dominant player in the market. In terms of volume, PSO accounts for 68% of total market share as of FY09, followed by Shell 12%, APL 7% and Caltex 5%. Furnace Oil (FO), High Speed Diesel (HSD), Motor Spirit (MS) and Jet fuel (JP) are major selling petroleum products.

In terms of volumetric sales of FO as of FY09, PSO held a market share of 86%, followed by APL (6%). Rest of the OMCs avoided dealing in FO due to persistence in circular debt issue. In case of MS, PSO had the major market share of 48%, followed by Shell (24%), Caltex (13%), Total Parco (9%) and APL (4%). Volumetric sales for HSD were also dominated by PSO with market share of 61%, followed by Shell (19%), Caltex (8%) and APL (4%). Jet Fuels were marketed by PSO (market share of 48%), Shell (35%), APL (7%) and Caltex (2%). In case of Asphalt, APL held the entire market share.

Volumetric Market Share (product wise)



Source: OCAC, BMA Research

Market share of PSO in Furnace Oil (FO) volumetric sales has increased significantly from 80.8% in FY07 to 86.4% in FY09. The reason behind this remarkable increase is the unwillingness of other OMCs (APL and Shell) in supplying FO to the power producing companies, due to the rising circular debt in the value chain.

On the other hand, since FY07 Shell has lost its share in HSD and MoGas to new OMCs (APL, Admore, Hascombe, Askar and Bosicor) by 405bps and 354bps respectively. 55% of Shell's volumetric offtakes come from HSD and 19% come from MoGas in which it holds the second largest market share (18% and 25% as of CY09 respectively). The reduction in market share is primarily attributed to a reduction in its number of retail outlets from 1088 in FY07 to 839 in FY09.

Over the next 5 year period we expect the two largest OMCs (PSO and Shell) to lose market share in HSD and MoGas (by 800bps and 500bps respectively) to new OMCs (APL, Admore, Hascombe, Askar and Bosicor), as these new OMCs aggressively expand their retail network. Moreover, resolution of circular debt issue will encourage APL and Shell to regain their market share in FO sales. Over the next 5 year period, we expect PSO to lose its market share in FO volumetric sales by 500bps.

ASPHALT: THE DARK MATTER

Asphalt contributes ~50% to the gross profit of APL and constitutes ~21% of its total volumetric sales. Asphalt being a high margin product, along with stability in its volumetric sales, stands out as the most important avenue for the company. Asphalt is used as bitumen for roads construction and is hence primarily demanded by contractors to Government Projects in Pakistan.

APL is the only OMC in Pakistan that deals in Asphalt and therefore has significant monopolistic power in the market.

Production dynamics

National Refinery Ltd (NRL) and Attock Refinery Ltd (ATRL) – both part of the Attock Group; are primary producers of Asphalt in Pakistan. Asphalt production is handled by lube section in the refineries and is a negative GRM product. It is produced almost at the end of the fractional distillation process and processed by the lube section.

Depending on the demand for the product, NRL and ATRL produce 5% to 9% of Asphalt out of each barrel of crude oil processed by them. The crude left behind after extraction of MoGas, HSD, Naptha, LPG and other high margin products is used as Furnace Oil, Asphalt or for manufacturing of other solvents and lubricants. As this part of the crude is not made up of certain length of carbon chain homogenous compounds, therefore it can be used for products made out of it interchangeably. Furnace Oil and Asphalt constitute bulk of the left over crude in fractional distillation process, and hence one product's production is directly dependent on the other's demand and margin.

There are various other dealers of Asphalt in the local market but APL maintains its position as an established company for marketing of Asphalt and is thus a regular supplier to High way authorities – specifically National Highway Authority (NHA) and Punjab Highway Authority (PHA).

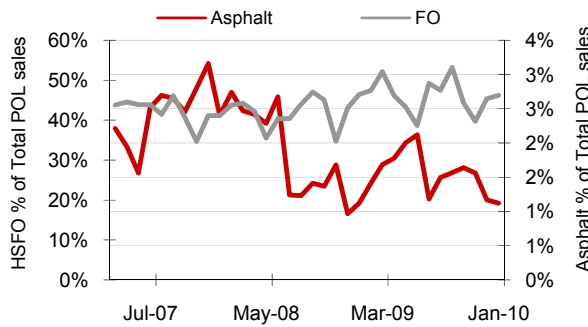
In order to discuss dynamics of Asphalt, we have tried to study its international and national historic trends. Prices, production and sales of asphalt are observed with various variables which can possibly impact supply and demand of the product.

Supply-side dynamics

Furnace Oil Demand

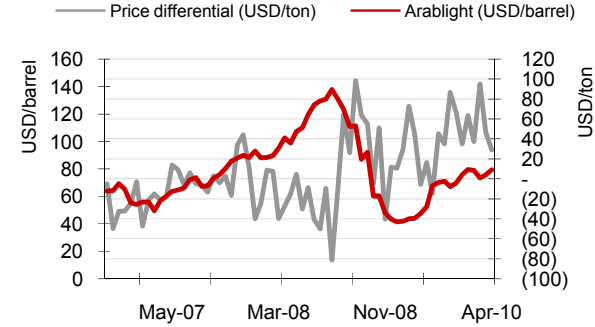
If furnace oil demand is high, it generates relatively greater Gross Refining Margin (GRM) ~-28% compared to that of Asphalt (~-32%); in which case refineries produce more of FO/bbl of oil at the expense of latter's production. In Pakistan's context, this is evident from inverse relationship between FO and Asphalt sales as percentage of total petroleum product's (POL) sales (correlation -0.43). However squeezed supply of Asphalt later creates upward pressure on its prices; as a result of which its GRM gets closer to that of FO. This is reflected by inverse relationship between Arab light prices and FO, Asphalt price differential. Hence high furnace oil demand promotes lagged positive effect on Asphalt margins to the refineries and dealers.

FO and Asphalt Sales as % of total POL sales in Pakistan



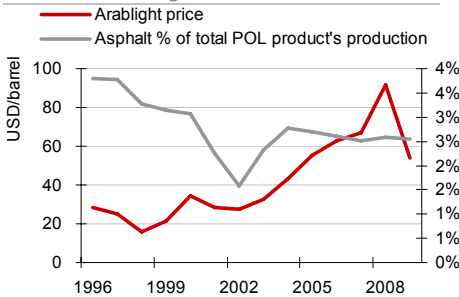
Source: OCAC, BMA Research

FO and Asphalt Price Differential vs Arab light Price



Source: California Department of Transportation, Bloomberg, BMA Research

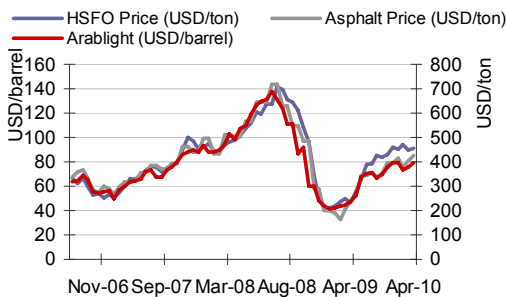
Asphalt % of total POL product's production in Pak vs Arab light Price



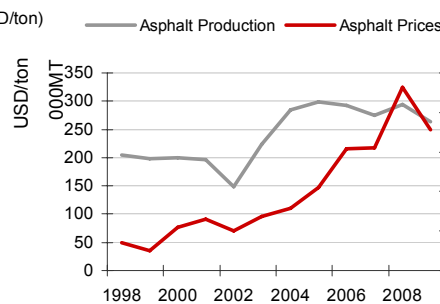
Crude oil prices: cost of oil has multiple impacts on Asphalt

- Rising oil prices provide incentive to produce high margin products (MoGas, HSD, JP, LDO and Naphtha) and less of FO and Asphalt, hence adversely affecting supply of Asphalt. In case of Pakistan, a weak correlation of -0.29 between Asphalt as a percentage of total production and Arab light crude oil price suggests that the above argument does not always hold true, hinting towards static demand in the country.
- Asphalt prices have high correlation of +0.97 with Arab light prices and +0.75 with Asphalt production suggesting that refinery's production of Asphalt is highly sensitive to Asphalt prices. This is also evident from direct relationship observed between Asphalt GRM and Arab light prices; higher GRM provides incentive to the refineries to produce more of Asphalt.

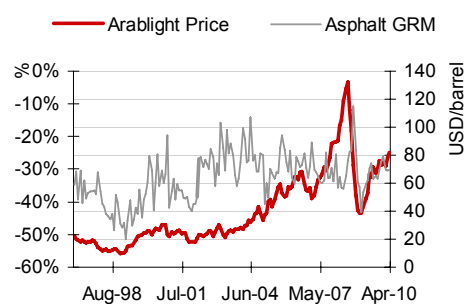
FO, Asphalt & Arab light Price History



Asphalt Prices vs Asphalt Production



Asphalt GRM% vs Arab Light Price



Source: Bloomberg, California Department of Transportation, BMA Research

Imports: In case of Pakistan there are no imports of Asphalt and the demand is catered through domestic production.

Summary

Rising oil prices have a net positive impact on Asphalt prices and supply. Although high value products are always preferred over Asphalt which puts its supply under pressure, the demand nonetheless remains relatively stable for the product. This eventually translates into a recovery in GRMs and supply for Asphalt.

Demand Dynamics

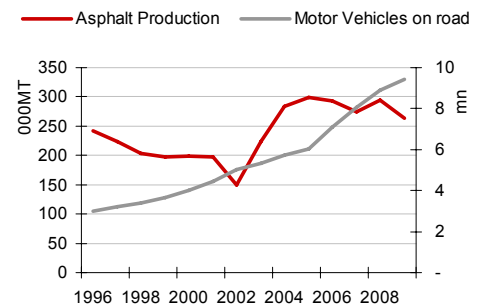
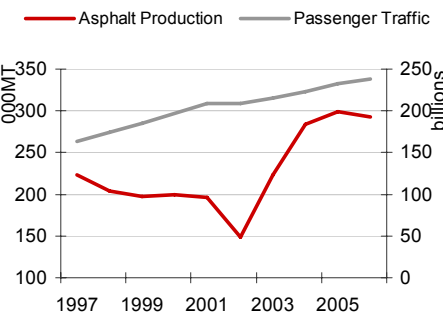
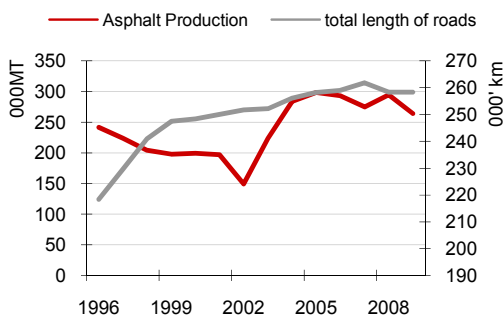
Transportation: Asphalt which is used in building infrastructure for transport, should intuitively be strongly related to transport activity. For this purpose we have analyzed the relationship of Asphalt production with various variables of transport activity. We have taken Asphalt production as a proxy variable for Asphalt sales, due to limitations of data availability. Recent historical observation suggests that Asphalt production and Asphalt sales are usually held in equilibrium. This makes Asphalt production a good proxy variable for Asphalt sales.

- **Length of Roads:** Asphalt production has a moderate positive correlation (+0.39) with the length of roads in Pakistan. This suggests that higher the length of roads, more the maintenance required and hence more of Asphalt is consumed.
- **Passenger Traffic:** Rising passenger traffic puts pressure on development authorities to rigorously maintain and expand the road network, which then fuels the demand for Asphalt. Moderate positive correlation (+0.58) between passenger traffic and Asphalt production in Pakistan supports this argument.
- **Motor Vehicles on Roads:** Motor Vehicles on the roads are a good proxy variable to passenger traffic as both the variables create the same pressure on development authorities. Rising motor vehicles on the roads eventually trigger higher demand for Asphalt as evident from positive correlation (+0.64) between motor vehicles on the roads and Asphalt production in Pakistan.

Total length of roads vs. Asphalt Production

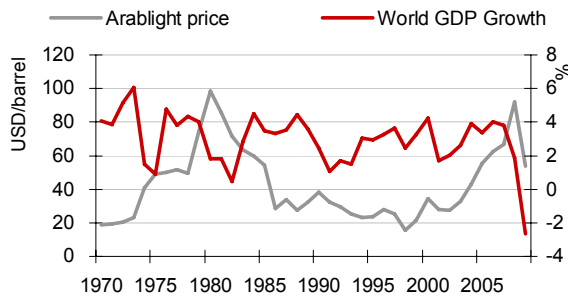
Passenger Traffic vs Asphalt Production

Motor Vehicle vs Asphalt Production



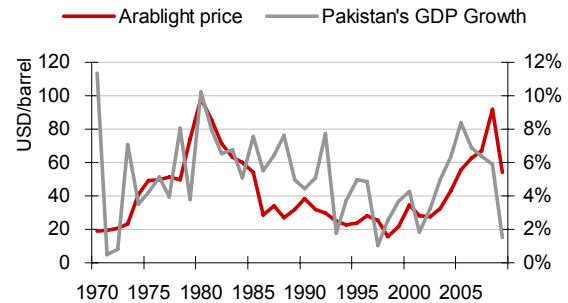
GDP Growth: There is a significant difference in the statistical relationship between the world's and Pakistan's GDP growth with Arab light prices. World GDP growth has a weak negative correlation of 0.23 with Arab light prices whereas Pakistan's GDP growth has moderate positive correlation of 0.41 with Arab light prices. This suggests that Pakistan's demand for Asphalt is likely to be high when Pakistan's GDP growth and Arab light prices are high.

World GDP Growth vs Arab light Price (inflation adjusted) History



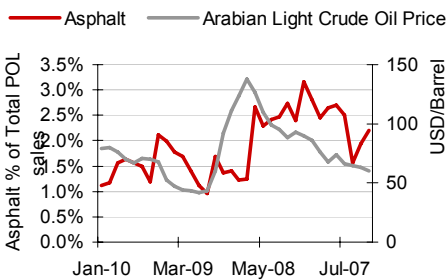
Source: United States Department of Agriculture, Bloomberg, BMA Research

Pakistan's GDP Growth vs Arab light Price (inflation adjusted) History



Source: United States Department of Agriculture, Bloomberg, BMA Research

Asphalt Sales as % of total POL sales vs crude prices



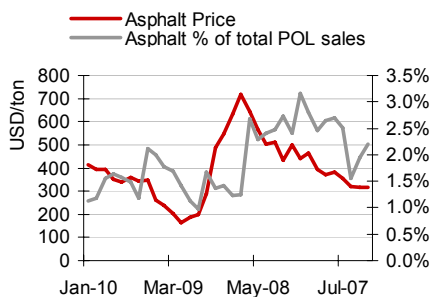
Crude oil prices: Low correlation (+0.19) of Asphalt sales as a % of total sales in Pakistan with Arab light crude oil prices suggests that Asphalt sales in case of Pakistan are fairly independent of crude oil prices. We believe this is due to stable Asphalt demand.

Price elasticity of Asphalt: Correlation of +0.23 between Asphalt price and Asphalt sales as a % of total sales and correlation of +0.20 between Asphalt price and Asphalt sales are moderately low suggesting significant inelasticity of demand.

Seasonality: Asphalt demand is high during dry hot seasons of the year and is the lowest during winters and rainy seasons. We believe this is due to technical applicability of Asphalt in road construction.

Marketing: In case of excess Asphalt production, active marketing done by dealers – specifically APL in case of Pakistan, also results in an artificial increase in demand to offset excess supply.

Asphalt Demand Sensitivity to Price



Other Considerations

Other factors which can possibly affect market dynamics of Asphalt but cannot be measured due to certain limitations include:

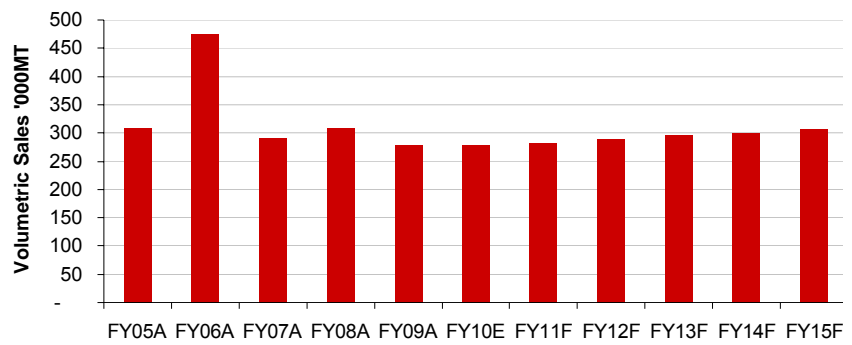
- Infrastructure Development budget and actual expenditure
- Inventory Levels of asphalt at local and international refineries
- Development budgets are fixed regardless of Asphalt Prices
- Infrastructure building activity abroad especially in Afghanistan

Source: California Department of Transportation, OCAC, Bloomberg, BMA Research

Future implications

We expect Asphalt demand and supply to remain stable going forward as it has been the case historically with little gap between supply and demand. Furthermore we expect its volumetric sales to grow at a CAGR of 2% for the next 5 year period on account of no major announcement by the GoP for infrastructure (road network) or building projects. Therefore growth in transport sector would majorly drive road maintenance activity.

Asphalt sales by APL

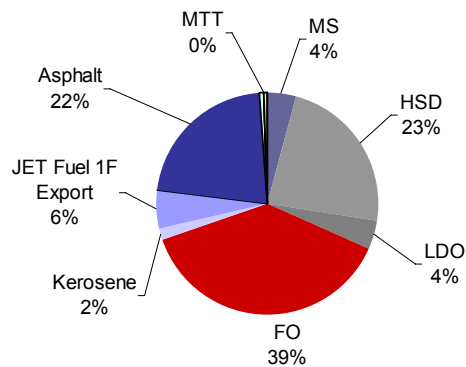


Source: OCAC, BMA Research

APL: THE CHANGING PIE

APL primarily markets Furnace Oil (FO), Asphalt, Kerosene (SKO), Light Diesel Oil (LDO), Solvent Oil, Lube Base Oil (LBO), High Speed Diesel (HSD), Petrol Motor Gasoline (MoGas), Mineral Turpentine Tar (MTT), Jute Batching Oil (JBO) and Waxes. During FY09, 39% of total volume sold was that of FO, followed by HSD (23%), Asphalt (22%), Jet Fuel (6%), Motor Spirit (4%), Light Diesel Oil (4%) and others (2%).

Product Share In Total Volume

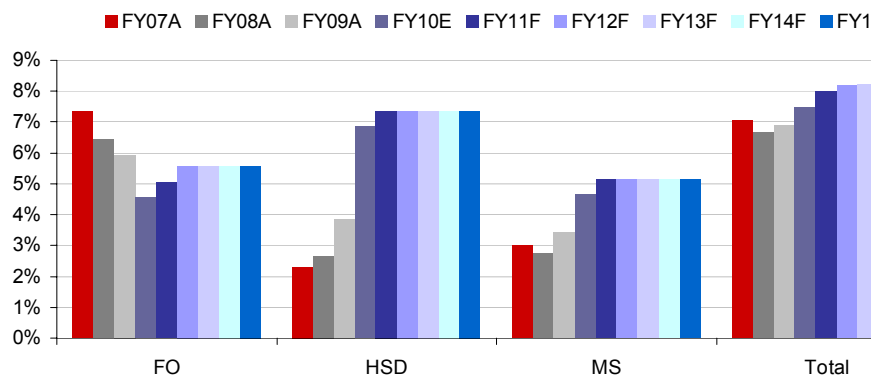


Source: OCAC, BMA Research

In terms of sales volumes sold during FY09, APL had total market share of 7%, after PSO (68%) and Shell (12%). Product wise sales in FY09 were as follows:

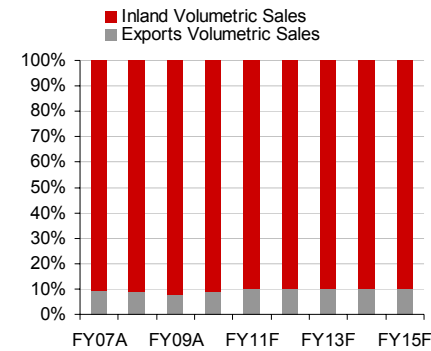
- **FO:** APL ranked 2nd with 6% market share. We expect that APL will lose its market share by 48bps by FY12, as demand for FO by IPPs and RPPs will increase. On the other hand APL will not cater to any additional demand due to persistence in circular debt issue
- **HSD:** APL ranked 5th with 4% market share; we expect the company to increase its market share by 350bps by FY11
- **Asphalt:** APL held the entire share of Asphalt sales amongst OMCs and is expected to continue to do so
- **MoGas:** APL ranked 5th with 3% market share; we expect APL to increase its market share further by 180bps by FY11

APL's Market Share



Source: OCAC, BMA Research

APL's Export and Inland POL volumetric sales mix

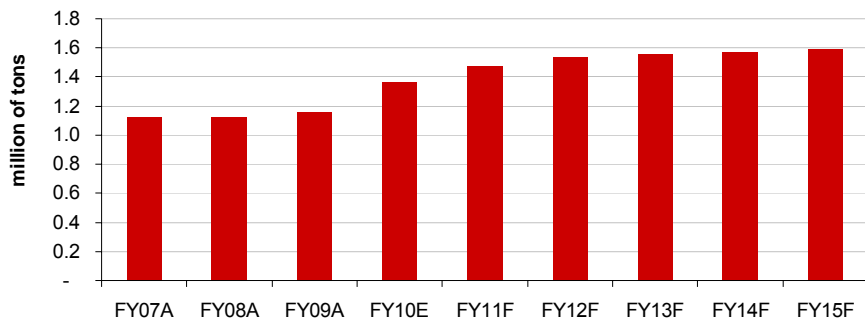


Source: OCAC, BMA Research

Inland and Export market share

Exports contributed 7.9% to APL's total volumetric sales during FY09. APL's total inland sales have experienced a modest growth during FY08-09 period growing at a CAGR of 3.0% against industry average CAGR of -1.2% over the same period. We expect the trend to continue and domestic volumetric sales to grow at a CAGR of 3% for the next 5-year period, in line with our expectations regarding its expansion strategies.

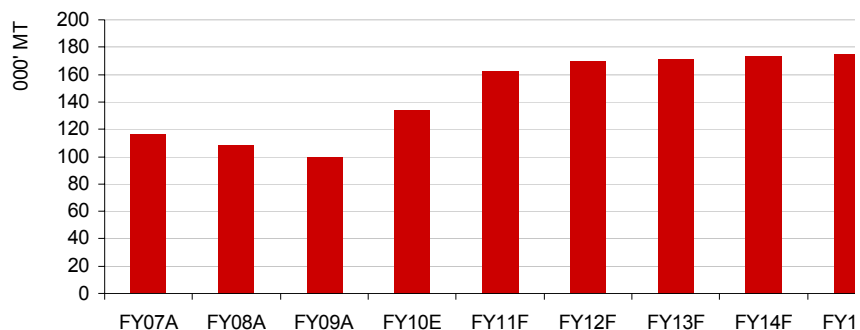
APL's Inland POL Volumetric Sales



Source: OCAC, BMA Research

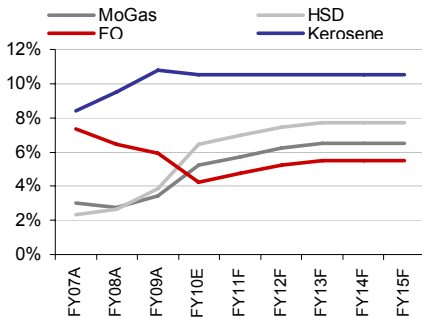
However, APL's exports have declined consecutively over the past 3 years (FY07 to FY09) at a CAGR of -7.3% against industry CAGR of 13.8%. This shows how rapidly APL is losing its export market share to its competitors, primarily to PSO and Shell. The primary reasons for this decline are: 1) APL is absent in import of Petroleum Products participation 2) Refineries are operating at low utilization rates due to circular debt issue as a result of which domestic supply of petroleum products is low 3) domestic demand for petroleum products is continuously rising. As a result domestic demand exceeds domestic supply and prioritizing local availability makes it difficult for APL to cater to the export market. We expect the trend to reverse going forward and estimate export volumetric sales to grow at a CAGR of 6% for the next 5-year period with the circular debt easing off and utilization rates of refineries recovering.

APL's Export POL Volumetric Sales

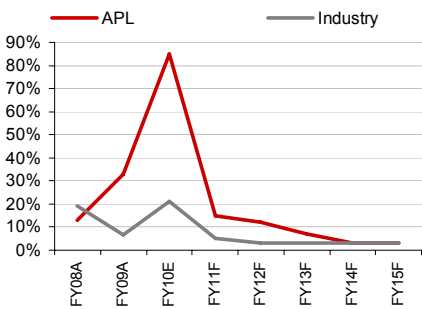


Source: OCAC, BMA Research

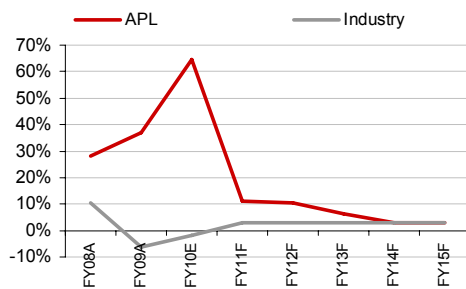
APL's Market Share Product wise



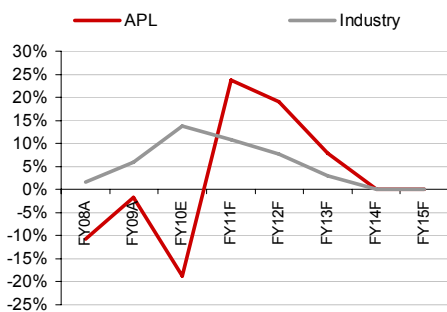
MS volumetric sales YOY change



HSD volumetric sales YOY change



FO volumetric sales YOY change



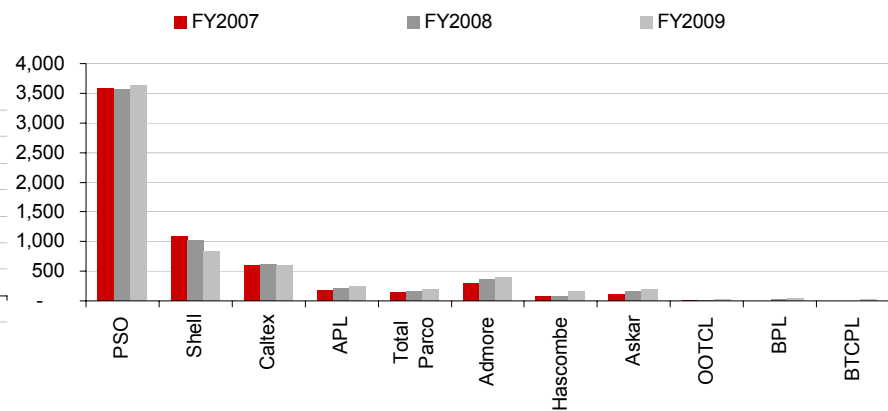
Source: OCAC, BMA Research

EXPANSION: SPREADING WINGS

Since its inception APL has adopted an aggressive expansion strategy. During the last 3 years APL has increased its number of retail outlets from 177 in FY07 to 246 in FY09, registering an annual growth of ~18%.

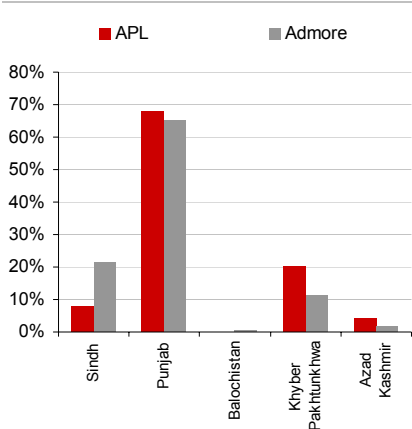
- APL now operates 3.9% of total retail outlets compared to 2.9% in FY07
- APL's volumetric market share in HSD, SKO and MoGas has increased over the past 3 years by 156bps, 238bps and 42bps respectively. We expect APL to further increase its market share over the next 5-year period in HSD and MoGas (by 351bps and 170bps respectively) as more stations come online. Additionally, market share in FO fell due to persistence in circular debt issue while APL is expected to regain some of its market share if the same is resolved. At the same time APL operated as a monopoly in asphalt and is expected to hold the same position amongst OMCs going forward
- APL's volumetric POL sales growth (3 yr CAGR of 6.1%) has outperformed industry (3 yr CAGR of 3.8%). Similarly sales of MS and HSD (major contributors to APL's gross margins) have also lately outpaced industry average. However the company has been a loser in FO market due to circular debt issue. It was wise on the part of APL to avoid FO or else the sales would have resulted in a liquidity crunch experience, similarly to PSO

Retail Outlets



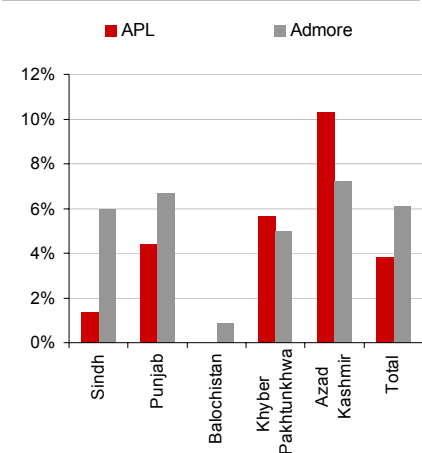
Source: OCAC, BMA Research

Retail Outlet Distribution



Source: OCAC, BMA Research

Market Share (Retail Outlets)



Source: OCAC, BMA Research

Acquisition of Admore

APL has recently shown interest in acquiring Admore Gas (Pvt) Ltd. This merger can have multiple impacts; though all positive on APL’s balance sheet and operating performance:

1. Geographic diversification and rapid expansion
2. Excess liquidity will be utilized
3. Increased Storage facility

Ad’more in reach

APL has a total of 246 retail outlets (4% of total retail outlets in Pakistan), whereas Admore has 390 outlets (6% of total retail outlets in Pakistan) currently functioning while 150 sites are under various stages of licensing and construction. Acquisition of Admore can provide 159% increase in the number of retail outlets to total at 636 operational retail outlets for APL. In addition, 65% of Admore’s outlets are in Punjab translating into 7% market share in terms of retail outlets present in the province. Further APL already has 68% of its outlets in Punjab; the acquisition would further strengthen APL’s presence there increasing its market share to 11% in terms of retail outlets.

Admore also has a significant representation in Sindh with 83 outlets, which is 6% of total retail outlets in the province, whereas APL has only 19 outlets or 1% of total retail outlets in Sindh. The acquisition can result in significant market share gains in Sindh. APL currently does not have any representation in Balochistan, however, Admore operates 2 petrol stations in the province, and the acquisition can give APL entry into this province. Acquisition can also result in a gain of 44 retail outlets in Khyber Pukhtunkhawa (50 currently operated by APL) and 7 retail outlets in Azad Kashmir (10 currently operated by APL).

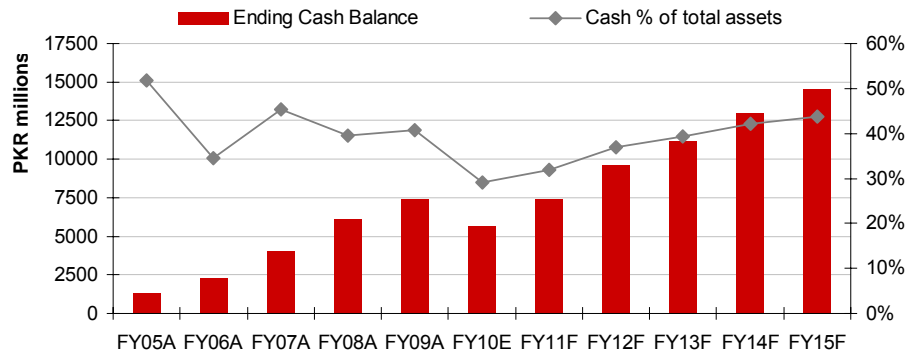
The hidden pot of gold

At present nothing can be said with conviction for the sales volumes for Admore, as the company has entered into Sale & Purchase agreements with Refineries & OMCs including Bosicor, PSO and OGDC for supply of various petroleum products at different depot locations. Further this has resulted into a biased sales data. Sales made by Admore and supplied by PSO are shown as sales for PSO rather than for Admore. Nonetheless APL can benefit from increased volumetric sales especially keeping APL’s synergies with the group in mind.

Utilize the Excess Liquidity

Historically and as per our forecast (without incorporating effects of acquisition) APL also has excess liquidity on its balance sheet both on absolute basis and with respect to its total assets. APL can utilize this excess cash for acquisition of Admore and put excess liquidity to better use. Historically, ROA and ROE for APL has been ~17% and ~44% respectively, given that ~40% of its assets were liquid in nature. So effectively APL’s return on non-cash assets has been ~29%, therefore utilizing this excess liquidity can boost ROA and ROE to 29% and 73% respectively.

Liquidity position of APL



Source: Company Reports, BMA Research

Increased Storage Facility

Admore’s current product transportation and supply facilities include:

- An agreement with PARCO for the usage of Mahmood Kot – Faisalabad Machike (MFM) Pipeline to receive products at Admore’s Bulk Oil Terminal at Machhike
- Agreement for usage of White Oil Pipeline (WOP) leading to Shikarpur and Machhike storage terminals

Admore’s storage facilities include:

- Al-Rahim Terminal in Keamari for receiving, storage and delivery of HSFO, HSD and PMG from southern refineries
- 32,000MTs storage facility for FO on ‘Long Lease’ (with option to buy) at Port Qasim
- Bulk oil storage facility at Machhike (near completion)
- Company has also acquired a piece of land at Mahmood Kot and is also planning to purchase land in Shikarpur to further increase the storage capacity

Acquisition of Admore will result in a significant increase in storage capacity for APL and synergies with already streamlined processes for transportation of products.

VALUATIONS & FINANCIAL FORECASTS

We have used Discounted Cash Flow (DCF) valuation method to assess the company. Using the DCF method, we have come up with a fair value of PKR545/share, assuming a terminal growth rate of 2%.

At yesterday's closing price of PKR293/share, APL currently offers an upside potential of 86% to our DCF-based fair value of PKR545/share. APL is attractively valued with FY11E PER of 4.7x. We recommend a BUY stance on the stock.

DCF Summary

PKR mn	FY10E	FY11F	FY12F	FY13F	FY14F	FY15F
EBIT	4,248	4,740	5,107	5,271	5,431	5,590
Tax	1,265	1,148	1,390	1,593	1,804	1,956
Non Cash Charges	509	392	427	453	482	513
Working Capital Investment	2,502	(321)	(557)	14	(237)	3
Fixed Capital Investment	(978)	(394)	(314)	(317)	(343)	(373)
Free Cash Flow	1,968	4,700	5,014	4,434	4,689	4,516
DCF Valuations						
PV of Forecasts						14,246
PV of Terminal Values						10,687
Value of Operating Assets						24,932
Value of Non Operating Assets						738
Enterprise Value						25,670
Value of outstanding debt						-
Equity Value						31,362
Number of outstanding shares						58
Per Share Fair Equity Value						545

Sensitivity Analysis

Sensitivity to WACC and Terminal Growth Rate					
Terminal Growth Rate	WACC				
	17.7%	18.7%	19.7%	20.7%	21.7%
1.0%	583	557	533	513	494
1.5%	591	564	539	518	498
2.0%	599	570	545	523	502
2.5%	608	578	552	528	507
3.0%	617	586	558	534	512

Balance Sheet

PKR mn	FY08A	FY09A	FY10E	FY11F	FY12F	FY13F	FY14F	FY15F
Current Assets	13,882	16,406	17,610	21,436	23,986	26,368	28,687	31,054
Fixed Assets	1,632	1,864	1,913	1,993	2,078	2,166	2,259	2,356
Total Assets	15,513	18,270	19,523	23,429	26,064	28,534	30,946	33,409
Current Liabilities	9,842	10,937	10,788	13,248	14,415	15,428	16,404	17,428
Long-term Liabilities	135	252	298	341	359	374	387	402
Total Shareholders Equity	5,536	7,082	8,437	9,839	11,290	12,732	14,154	15,579
Total Equities and Liabilities	15,513	18,270	19,523	23,429	26,064	28,534	30,946	33,409

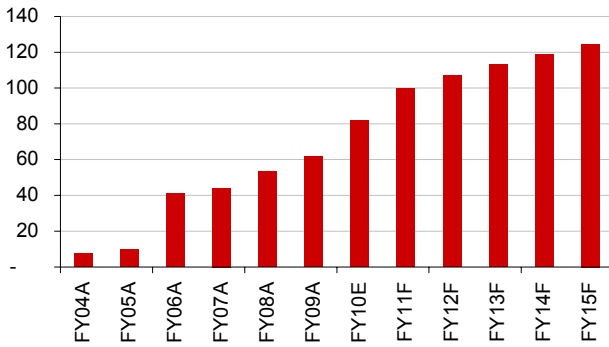
Income Statement

PKR mn	FY08A	FY09A	FY10E	FY11F	FY12F	FY13F	FY14F	FY15F
Net Sales	53,242	61,863	82,017	99,699	107,019	113,018	118,637	124,586
% ▲	20.70%	16.2%	32.6%	21.6%	7.3%	5.6%	5.0%	5.0%
Cost of Goods Sold	50,494	58,571	78,637	95,904	102,817	108,588	113,991	119,712
Gross Profit	2,748	3,292	3,379	3,795	4,202	4,431	4,646	4,874
Operating Expenses	478	649	832	762	856	952	1,061	1,186
Other Operating Income	896	844	866	832	849	867	885	904
Operating Profit	3,167	3,487	3,413	3,865	4,195	4,346	4,470	4,592
Other Income	382	849	944	1,002	1,052	1,105	1,160	1,218
EBITDA	3,549	4,336	4,357	4,867	5,247	5,451	5,630	5,810
Depreciation & Amort.	77	83	127	143	158	176	196	219
EBIT	3,472	4,254	4,229	4,724	5,089	5,275	5,434	5,592
Share of profits of ass.	59	27	19	16	17	19	21	23
PBT	3,530	4,280	4,248	4,740	5,107	5,294	5,455	5,615
Tax	888	1,198	1,065	1,148	1,390	1,600	1,812	1,965
PAT	2,642	3,082	3,183	3,592	3,717	3,694	3,643	3,650
EPS (PKR)	45.88	53.51	55.26	62.36	64.52	64.13	63.25	63.36
% ▲	52.9%	16.6%	3.3%	12.8%	3.5%	-0.6%	-1.4%	0.2%

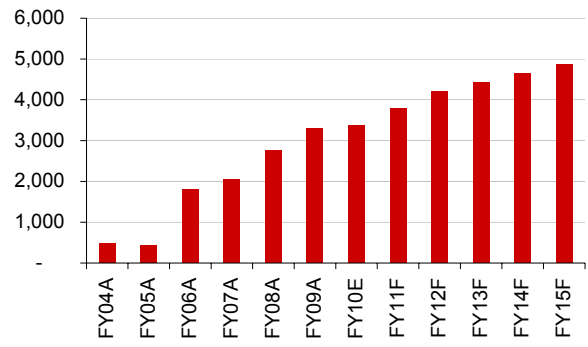
Key Ratios

Key Ratios	FY08A	FY09A	FY10E	FY11F	FY12F	FY13F	FY14F	FY15F
EPS (Rs)	45.9	53.5	55.3	62.4	64.5	64.1	63.2	63.4
Sales per share	924	1,074	1,424	1,731	1,858	1,962	2,060	2,163
Sales Growth	20.7%	16.2%	32.6%	21.6%	7.3%	5.6%	5.0%	5.0%
Payout Ratio	32.4%	52.9%	60.9%	60.9%	60.9%	60.9%	60.9%	60.9%
EPS growth	52.9%	16.6%	3.3%	12.8%	3.5%	-0.6%	-1.4%	0.2%
Profitability Ratios								
Net Margin	5.0%	5.0%	3.9%	3.6%	3.5%	3.3%	3.1%	2.9%
Gross Margin	5.9%	5.6%	4.2%	3.9%	3.9%	3.8%	3.8%	3.7%
Op Margin	5.9%	5.6%	4.2%	3.9%	3.9%	3.8%	3.8%	3.7%
EBITDA margin	0.1%	0.1%	0.2%	0.1%	0.1%	0.2%	0.2%	0.2%
Multiples								
PER (x)	3.8	NM	6.1	6.9	5	4.8	5.4	5.3
EV/EBITDA (x)	4.1	3.4	3.4	3.0	2.8	2.7	2.6	2.5
BVPS (PKR)	96.1	123.0	144.6	168.9	194.2	219.2	244.0	268.7
Price/Book (x)	1.7	2.6	1.9	1.5	1.2	0.9	0.8	0.7
DPS (PKR)	14.9	28.3	33.7	38.0	39.3	39.1	38.5	38.6
Dividend Yield	1.7%	1.7%	1.0%	0.9%	1.2%	1.3%	1.2%	1.2%
FCF/share (PKR)	45.2	48.8	0.2	67.9	76.2	66.1	69.8	65.8
Price/FCF(x)	13.7	14.7	38.6	(3.0)	5.3	2.3	2.3	4.6
ROE	47.7%	43.5%	38.2%	36.9%	33.2%	29.3%	25.9%	23.6%
Debt /Equity	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
ROA	17.0%	16.9%	16.3%	15.3%	14.3%	12.9%	11.8%	10.9%
Other								
Trade debtors, % of gross sales	9.7%	11.1%	9.7%	9.7%	9.7%	9.7%	9.7%	9.7%
Creditors & other liabilities % of gross sales	16.0%	14.6%	10.6%	10.6%	10.6%	10.6%	10.6%	10.6%
Stock-in-trade, % of gross sales	0.5%	0.2%	1.7%	1.2%	0.7%	0.7%	0.5%	0.5%

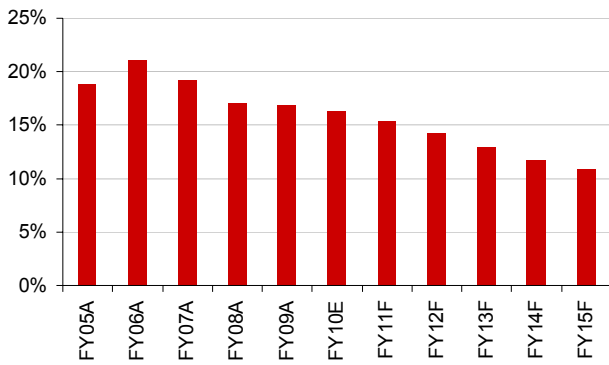
Net Sales (PKR bn)



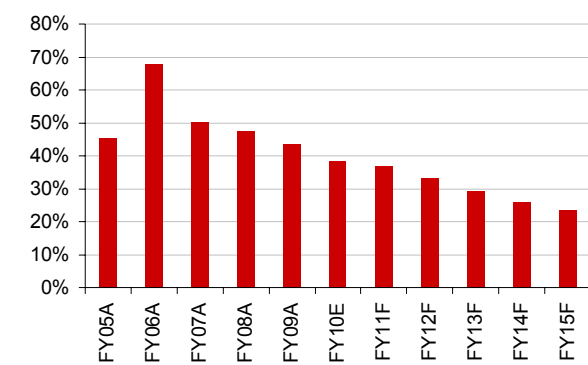
Gross Profit (PKR mn)



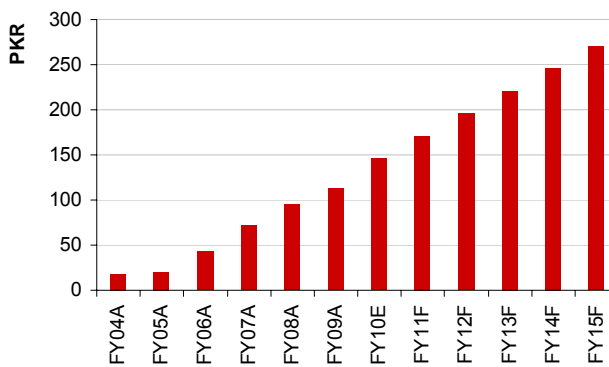
ROA



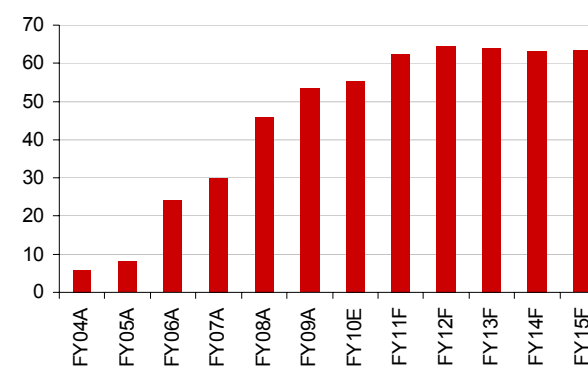
ROE



Break Up Value per share



EPS (PKR)



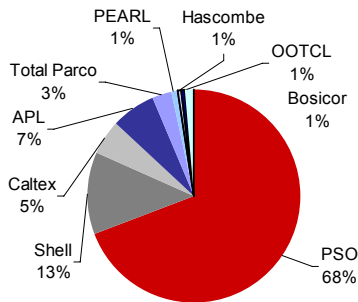
Source: SBP, BMA Research

Source: SBP, BMA Research

APL: ABOUT THE COMPANY

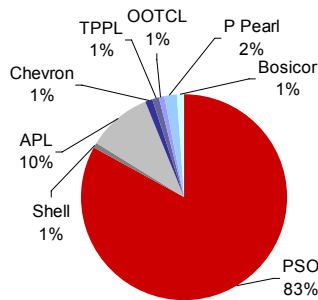
Attock Petroleum Limited (APL) was incorporated in Pakistan as a Public Limited Company on Dec 03, 1995, commenced operation in Feb98 and was listed on Karachi Stock Exchange on 07 Mar, 05. It is the 4th largest OMC after PSO (68%), Shell (13%), and Caltex (5%). APL being a relatively new entrant has managed to rapidly expand its retail network. The company is now ranked as the 3rd largest OMC of Pakistan in terms of aggregate Petroleum Oil & Lubricants sales and aggregate market share. Further APL had 10% share in Black Oil market and 4% in white oil market as of Jun09.

Total Market Share (Vol) – FY09



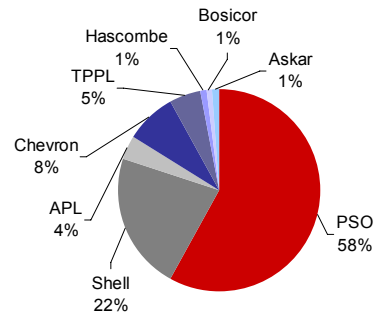
Source: OCAC, BMA Research

Black Oil Market Share – FY09



Source: Company Reports, BMA Research

White Oil Market Share – FY09

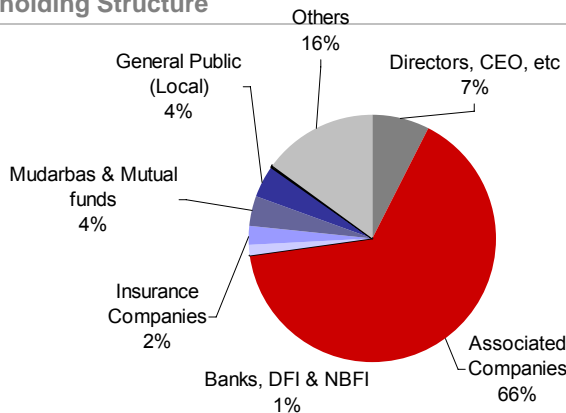


Source: Company Reports, BMA Research

Synergies with the Attock Group of Companies

APL is an associated member of Attock Group of Companies, a fully vertically integrated group in the field of Oil and Gas sector of Pakistan. The group holds stake in exploration, production, refining and marketing of a wide range of Petroleum Products. Additionally, its associated companies including Pharaon Investment Group Limited Holdings (PIGL) and Attock Oil Group of Companies together hold 65.5% stake in the company while only 4.3% equity is held by the general public.

Shareholding Structure



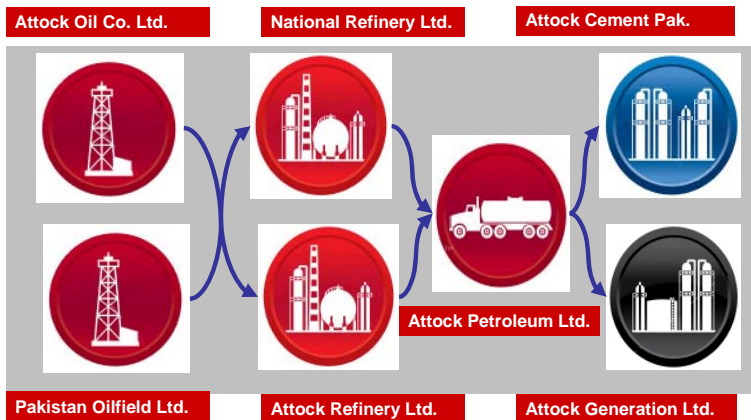
Source: Company Reports, BMA Research

Attock Group of Companies consists of:

- **Attock Oil Company Limited (AOC),**
- **Pakistan Oilfields Limited (POL),**
- **Attock Refinery Limited (ATRL),**
- **National Refinery Limited (NRL),**
- **Attock Cement Pakistan Limited (ACPL),**
- **Attock Generation Limited (AGL).**

APL possesses high synergies with its parent group and is therefore well positioned as far as petroleum products supplies are concerned. With two strategically located refineries: ATRL in the north and NRL in the south of the country; APL can ensure smooth product availability to its customers.

Attock Group of Companies



Source: BMA Research

Storage Terminals

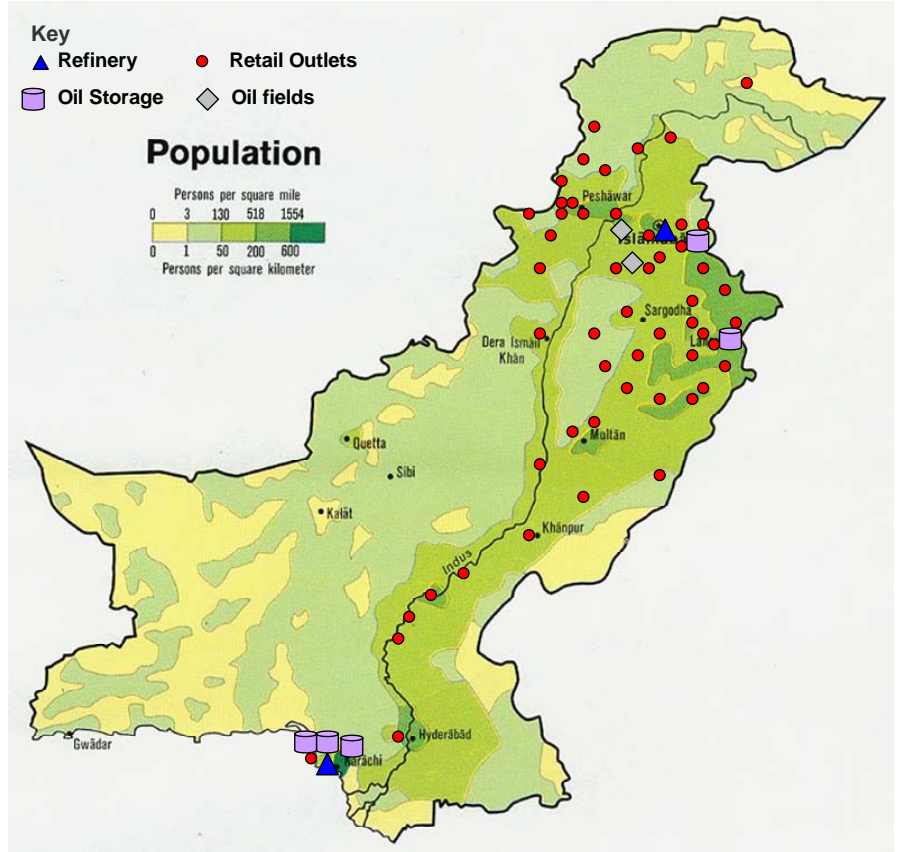
APL has a wide storage network which is strategically located nationwide. Some of the terminals are company owned and the rest are on hospitality basis. Terminals for APL include:

- Rawalpindi Bulk Oil Terminal (RBT), Rawalpindi
- Korangi Bulk Oil Terminal, Karachi
- Panama Oil Terminal, Karachi
- Keamari (Naptha), Karachi
- Machike Bulk Oil Terminal

RBT has storage facilities for High Speed Diesel, Premier Motor Gasoline, Kerosene Oil and Furnace Oil. Also, it is connected with ATRL through a pipeline from which storage tanks receive the products. Terminal also has a calibration facility for tank lorry calibration. APL has recently increased filling capacity at RBT by adding two new filling points, each for petrol and diesel.

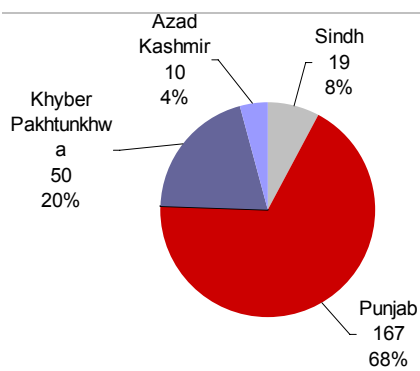
Machike bulk oil terminal has been recently commissioned near Lahore. APL is also ready to utilize White Oil Pipeline Project (WOPP) and will receive products on immediate basis at Gatti & Machike Installations. It has signed a deal with Pak Arab Refinery Limited (PARCO) and Pak Arab Pipeline Company Limited (PAPCO) for supplying its petroleum products through the White Oil Pipeline (WOP) and the Mehmoodkot-Faisalabad-Machike (MFM) Pipeline to facilitate the mid-country supply for customers.

APL's Products Network



Source: Company Website, BMA Research

APL Retail Outlets



Source: OCAC, BMA Research
 *APL has no representation in Baluchistan

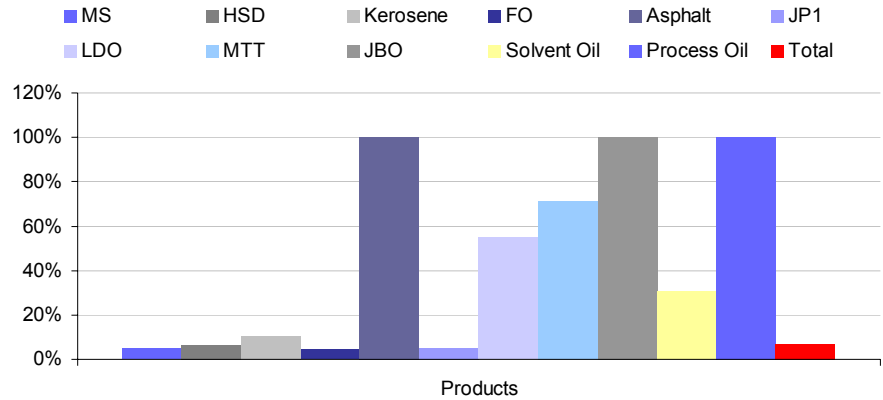
Retail outlets

APL has been aggressively expanding its retail network over the past few years and is expanding it in all directions: highways, urban and rural areas. Company retail outlets as of Jun 30, 09 stood at 246; by Dec, 09, APL was able to commission an additional 19 outlets bringing the number of retail outlets to a current total of 265.

Products

APL primarily markets Furnace Oil, Asphalt, Kerosene, Light Diesel Oil, Solvent Oil, Lube Base Oil, High Speed Diesel, Petrol Motor Gasoline, Mineral Turpentine Tar, Jute Batching Oil and Waxes. These products are marketed throughout Pakistan by selling both to the end users and industries.

APL's Market Share



Source: OCAC, BMA Research

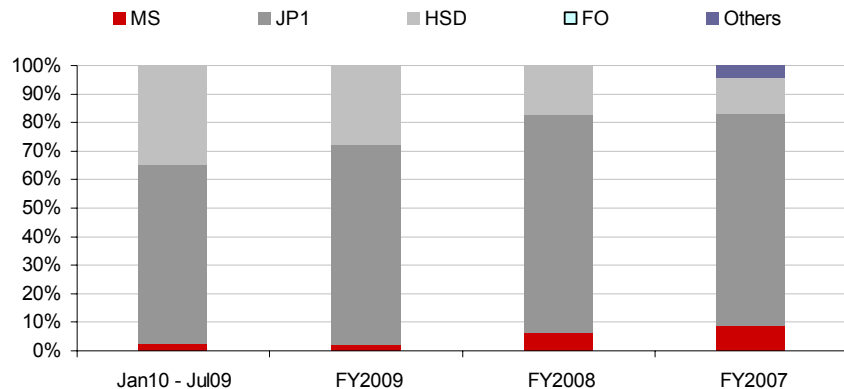
Lubricants

APL also has its own brand of lubricants in the market and offers a wide range of lubricants for gasoline, diesel and industrial consumers. The company has also made third party arrangements for local blending and is expanding its network of distribution to all major cities of Pakistan. Presently these products are being marketed in NWFP, Punjab and Sindh.

Exports

APL has been exporting petroleum products to Afghanistan since April 03 and has gained a significant share in export market. It is the first and the only OMC registered with Afghanistan Investment Support Agency (AISA) to operate in Afghanistan as a foreign company. Products currently being exported to Afghanistan include Premier Motor Gasoline (PMG), Jet Fuels (JP-8), and High Speed Diesel (HSD). APL is also a major exporter of Naphtha to Middle-East and Far-East countries. Approximately 336,000 MT of Naphtha is exported annually.

APL's Export Mix



Source: OCAC, BMA Research

Future Plans

APL intends to dominate the southern region of the country and for this it plans to:

- Develop Retail outlets in high trade areas which includes highways, urban & semi-urban centers
- Set up a Lubricant Blending Plant and increase its focus on marketing of Gasoline/Diesel Engine Oils and Industrial Lubricants
- Huge capital re-injection for conversion of old vision retail outlets into new retail visual identity (RVI)
- Expansion of consumer base in other petroleum products locally and globally
- Further increase storage capacity of existing bulk oil terminal at Rawalpindi

APL has shown willingness to buy 100% shares of ADMORE Gas Pvt Limited in order to diversify and expand geographically. This acquisition can provide inorganic growth and significant gains in market share.

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ANALYST CERTIFICATION

I, Muhammad Ali Taufiq, hereby certify that this report represents my personal opinions and analysis of information. All views are accurately expressed to the best of my knowledge. I certify that no part of my remuneration is linked either directly or indirectly to recommendations or analysis covered in this report.